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OUR STRATEGY IS
SOUND

PATHEON

Highlights of the Year

March 2001

Patheon signs agreement with Novartis Pharmaceuticals Canada Inc. to provide long-term manufacturing and supply services to Novartis and to purchase Novartis' manufacturing facility in Whitby, Canada. The agreement was completed on April 30, 2001.

Patheon expands its Pharmaceutical Development Services capacity at Toronto Region Operations with the opening of a new formulation development facility. The state-of-the-art addition enables Patheon to move clients' products through early development more quickly and cost effectively.

May 2001

Patheon UK Limited signs agreement with Weston Medical Group plc to provide development and commercial manufacturing services for Intraject®, Weston's needle-free drug delivery system. Patheon will become the preferred manufacturer of Intraject® pre-filled capsules for pharmaceutical and biotechnology companies that have licensed the technology from Weston Medical.

June 2001

Ronald B. Mitchell, C.A., is appointed Senior Vice-President, Finance & Treasurer, responsible for managing the Corporation's finance, treasury and financial reporting functions.

Patheon enters into a bought-deal common share financing led by RBC Capital Markets to sell 3,400,000 common shares (including underwriters' over-allotment) at a price of \$14.65 per share, for total gross proceeds of \$49,810,000.

2001 Financial Highlights

For the years ended October 31

(in thousands of Canadian dollars except share information, per-share amounts and percentages)

	2001 \$	2000 \$	% Change
CONSOLIDATED STATEMENTS OF EARNINGS			
Revenues	319,877	256,309	25%
Earnings before interest, taxes, depreciation and amortization (EBITDA)	41,433	34,150	21%
% of revenues	13.0%	13.3%	
Earnings before income taxes	25,739	21,135	22%
Provision for income taxes	9,418	7,584	24%
Net earnings	16,321	13,551	20%
PER SHARE INFORMATION			
Earnings per share			
Basic	0.34	0.31	10%
Diluted	0.33	0.30	10%
Cash flow from operations per share	0.69	0.58	19%
Weighted average number of shares outstanding (basic)	47,924	43,438	10%
BALANCE SHEET			
Total assets	353,174	243,242	45%
Working capital	11,803	5,828	103%
Interest-bearing debt	51,302	46,540	10%
Shareholders' equity	198,296	124,431	59%
Return on shareholders' equity	10.4%	15.8%	
Interest-bearing debt to shareholders' equity	25.9%	37.4%	
Interest-bearing debt to total capitalization	20.6%	27.2%	
Book value per share at year-end	3.94	2.70	46%
Number of employees at year-end	2,581	1,914	35%

Highlights of the Year

June 2001

Patheon opens a Pharmaceutical Development Services facility at its site in Swindon, United Kingdom. With PDS capabilities in Toronto and Swindon, Patheon can now provide development services in both North America and Europe and for a wide range of dosage forms, including sterile products.

July 2001

Clive V. Bennett is appointed Executive Vice-President, International Operations. Mr. Bennett has more than 30 years of industry experience, formerly serving as Senior Vice-President, Operations and Head of Global Drug Product Supply for Hoechst Marion Roussel (now Aventis). He joined Patheon's Management Advisory Board in January 2000, providing strategic counsel on current developments in the global pharmaceutical industry.

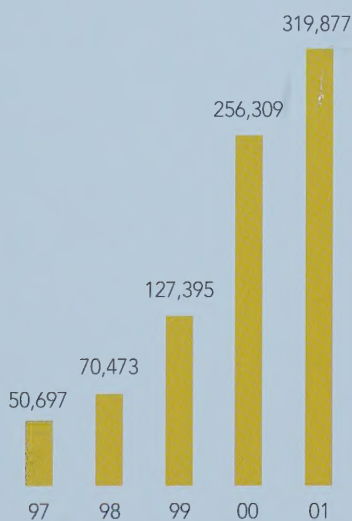
December 2001

Patheon announces results for the year ended October 31, 2001. Revenues increased 25% to \$319,877,000 and EBITDA (earnings before interest, taxes, depreciation and amortization) rose 21% to \$41,433,000. Net earnings increased 20% to \$16,321,000 and earnings per share (basic) increased 10% to 34 cents.

Five-Year Summary

REVENUES

(in thousands of Canadian dollars)

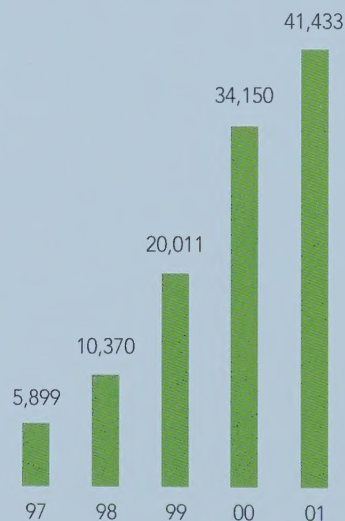


CAGR
58%

Revenues grew to \$319.9 million this fiscal year and, over the past five years, have increased at a compound annual growth rate of 58%.

EBITDA

(in thousands of Canadian dollars)

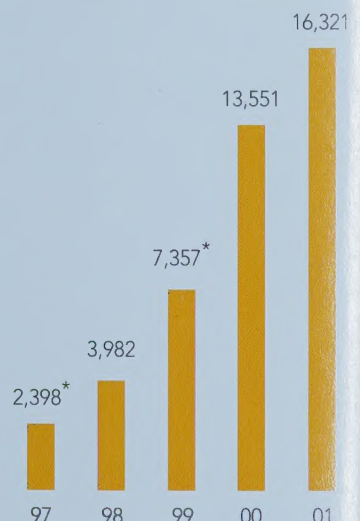


CAGR
63%

Earnings before interest, taxes, depreciation and amortization have continued to grow consistently, increasing to \$41.4 million in fiscal 2001.

NET EARNINGS

*(before unusual items)
(in thousands of Canadian dollars)



CAGR
62%

Net earnings reached \$16.3 million in fiscal 2001, marking another successful year of profitable growth.

Patheon is a leading global provider of drug development and manufacturing services to the international pharmaceutical industry. Exclusively focused on outsourcing, Patheon offers complete and fully integrated solutions, from developing dosage forms for new drugs through to commercial manufacturing of finished products.

With nine facilities and more than 2,500 employees in North America and Europe, Patheon has the capacity, expertise and reach to serve the growing outsourcing needs of the global pharmaceutical industry.

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OUR STRATEGY

is to become the preferred outsourcing partner worldwide of the industry's innovators – the global pharmaceutical companies, biotechs and emerging marketing companies that are bringing new pharmaceutical products to market.

Patheon an international leader in the contract manufacturing and development of pharmaceutical products across all therapeutic categories.

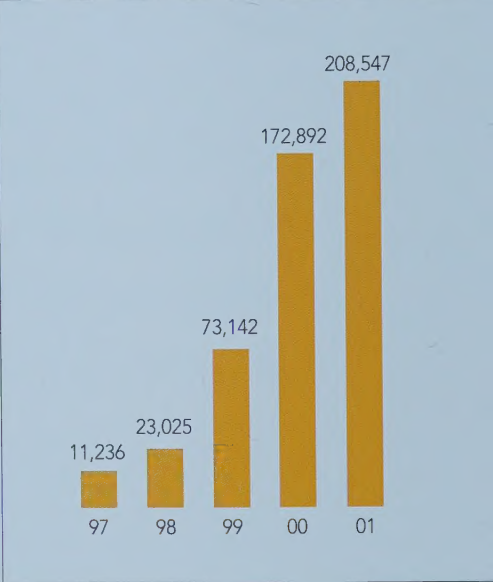
PDS

PHARMACEUTICAL
DEVELOPMENT
SERVICES



Rx

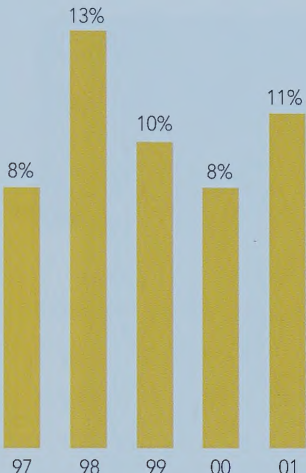
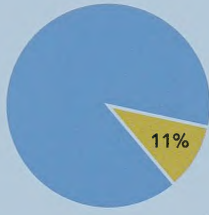
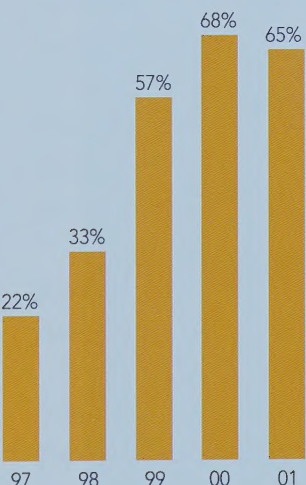
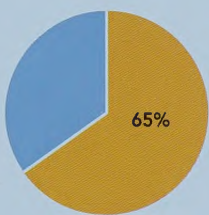
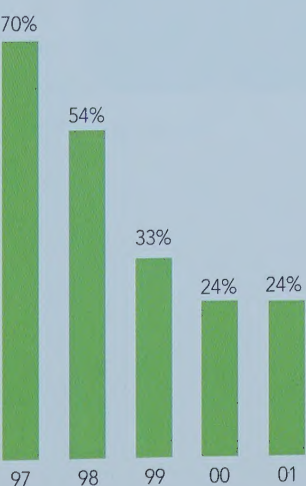
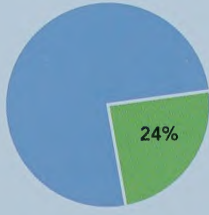
COMMERCIAL
MANUFACTURING
OF PRESCRIPTION
PRODUCTS



OTC

COMMERCIAL
MANUFACTURING
OF OVER-THE-COUNTER
PRODUCTS



Percentage of Total Revenues	Percentage of Total Revenues in 2001	2001 Achievements	2002 Objectives																		
 <table><caption>Percentage of Total Revenues (1997-2001)</caption><thead><tr><th>Year</th><th>Percentage</th></tr></thead><tbody><tr><td>97</td><td>8%</td></tr><tr><td>98</td><td>13%</td></tr><tr><td>99</td><td>10%</td></tr><tr><td>00</td><td>8%</td></tr><tr><td>01</td><td>11%</td></tr></tbody></table>	Year	Percentage	97	8%	98	13%	99	10%	00	8%	01	11%	 <table><caption>Percentage of Total Revenues in 2001</caption><thead><tr><th>Category</th><th>Percentage</th></tr></thead><tbody><tr><td>Other</td><td>89%</td></tr><tr><td>Specific</td><td>11%</td></tr></tbody></table>	Category	Percentage	Other	89%	Specific	11%	> Expanded formulation development capacity in Toronto and opened new PDS facility in Swindon, UK > Added more than 70 PDS staff in Toronto and Swindon > Five PDS Rx products were launched by our clients and moved to commercial manufacturing with Patheon > PDS revenues increased by 58% over fiscal 2000	> Expand PDS by internal growth and acquisitions > Continue to add scientific expertise > Broaden range of value-added services
Year	Percentage																				
97	8%																				
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Year	Percentage																				
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01	24%																				
Category	Percentage																				
Other	76%																				
Specific	24%																				

SOUND
STRATEGY
STRONG
RESULTS

Message to Shareholders



ROBERT C. TEDFORD
CHIEF EXECUTIVE OFFICER

PETER A. W. GREEN
CHAIRMAN OF THE BOARD



Fiscal 2001 marked another outstanding year for your Company.

- We added a ninth commercial manufacturing facility, accompanied by long-term contracts, to our business;
- We enhanced our growing pharmaceutical development services (PDS) business with additional people, facilities and services; and
- We were selected as commercial manufacturers of a number of newly launched prescription products for which we had provided development services.

We strengthened our leadership positioning with these initiatives while delivering yet another year of double-digit growth in revenues and net earnings.

For the year ended October 31, 2001, we achieved revenues of \$319.9 million, a 25% increase from \$256.3 million in fiscal 2000. Earnings before interest, taxes, depreciation and amortization (EBITDA) grew 21% to \$41.4 million, and the EBITDA margin was 13.0%, compared with 13.3% last year. Net earnings rose 20% to \$16.3 million, while basic net earnings per share grew to \$0.34 from \$0.31 a year earlier. Cash flow from operations of \$33.1 million was 32% higher than a year ago.

For the full year, revenues increased by \$63.6 million. Of this increase, 79%, or \$50.4 million, was strategic growth, resulting principally from the long-term contracts signed in connection with the acquisition of the Whitby site in Canada from Novartis in April of 2001. Organic growth, defined as new business obtained for our existing sites, represented 21%, or \$13.2 million.

Our North American facilities continued to generate strong results. In fiscal 2001, we achieved net organic revenue growth of 19% in North America, representing mainly higher-value pharmaceutical development services (PDS) and prescription (Rx) manufacturing business.

In the European Economic Community, we are beginning to attract new business to all three of our sites – in Italy, where we initially established our presence in early 1999, and in the UK and France, where we acquired two more facilities in December of 1999. In fiscal 2001, our European Rx revenues grew 8%, but overall growth was 2% after reflecting the decline in volumes of over-the-counter (OTC) products, some of which resulted from our decision to discontinue manufacturing products for clients which had inadequate returns. Net growth was also affected by a higher-than-expected decline in certain mature products.

These European growth rates are modest and well below our experience in North America. We are not satisfied with these results and are therefore strengthening our marketing and sales efforts to better penetrate the fragmented market in Europe. We are also making capital investments to enhance our higher value-added manufacturing activities. In June 2001, for example, we opened a PDS facility at our UK manufacturing site. We are also investing in the expansion of our lyophilization capacity at our site in Italy. We remain confident that this focused strategy will generate improved results, and we remain committed to growing our integrated development and manufacturing services in Europe as we have done in North America.

In 2001, all service activities contributed solid growth. Revenues from our PDS business – Patheon's fastest growing service activity – increased 58%. Commercial manufacturing revenues increased 22%, with Rx up 21% and OTC up 25%. Representing 24% of our total revenues, OTC manufacturing remains an important part of our business, where we are focusing on well-known brands of consumer products with higher volumes.

An Exciting New Era

Over the last 27 years, we have earned the confidence of our clients by manufacturing their commercial products to their exacting quality standards and expectations. Today, we are supporting them in the development of new, patented drug products. This is the beginning of an exciting new era for Patheon. Here's why.

Products in development build value in two ways. First, they generate higher-quality earnings. Second, as our PDS business continues to grow with more and more products in development, so will our opportunities to be selected as the commercial manufacturer of new higher-volume, top-selling products. The earlier in its lifecycle that a product enters the Patheon pipeline, the longer its potential revenue stream.

Today, we have a staff of almost 200 involved in PDS service activities, from the development of formulations for clinical trials of new products through scaling up to commercial quantities for product launches for our clients. During fiscal 2001, Patheon's PDS pipeline continued to grow, with an ever-increasing number of clients' products in development. At the end of our fiscal year, we had 40 products under development on behalf of our clients, including 5 in preclinical testing, 19 in Phases I and II of clinical trials, 11 in Phase III, and 5 awaiting regulatory approval. In fiscal 2001, five Rx products that had been in our development laboratories were launched by our clients and produced in our commercial manufacturing facilities.

A Sound Strategy

Over the course of the next five years, we expect to be operating from a much larger platform with a solid global presence and an ever-widening base of integrated development and commercial manufacturing services.

We will continue to seek facilities that complement our broad capabilities, augment our capacity and are accretive to earnings within the first year. A priority for your Company is to acquire high-quality, sophisticated manufacturing facilities with highly trained people in the U.S. from which we can offer our integrated PDS and commercial manufacturing services. We have a sound balance sheet, are generating significant cash flows and judiciously reinvesting to assure more profitable future growth and stronger cash flows.

Message to Shareholders

Based on current forecasts of requirements from our existing clients and on current expectations of new revenue opportunities, revenues in fiscal 2002 are expected to approach \$400 million. In addition, we remain committed to improving the quality of earnings by achieving higher utilization of existing manufacturing capacity and focusing on attracting higher value-added business, particularly in Rx and PDS activities.

We are building our operating infrastructure to position us to manage our growth. We have a successful record of acquiring, transforming and integrating manufacturing sites into our global network, and are very pleased with the progress we have made in this regard with our latest acquisition from Novartis in Canada. We are strengthening your Company not only with the people who join us through our site acquisitions but also with successful efforts to recruit talent at all levels of the organization, in the areas of operations, science, quality, sales, marketing, and finance.

We are pleased that Mr. Rudolf Meyer, formerly a senior global manufacturing executive with F. Hoffmann-La Roche, has joined our Management Advisory Board. Mr. Clive Bennett, who was a member of our Advisory Board, has accepted a full-time position with your Company and is now Executive Vice-President, Operations. Mr. Bennett previously served as head of global drug product supply for a major pharmaceutical company, overseeing 35 sites and 10,000 employees.

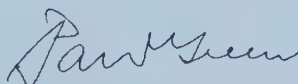
Word of the Year

As a growing organization, we are constantly striving to raise and surpass the bar. This is a challenge that we embrace at every level of our organization. With a sound strategy focused on our three vectors for growth – more higher-value services, more early-lifecycle products in commercial manufacturing and more commercial manufacturing capacity – we are confident that we will continue to create *long-term economic value for our shareholders*.

We thank, first of all, our people for their energetic efforts to meet the needs of our clients for exceptionally high-quality services. We thank our clients for entrusting us with their business. And we thank you, our shareholders, for your continued support.



CHIEF EXECUTIVE OFFICER



CHAIRMAN OF THE BOARD

February 5, 2002

1

MORE HIGHER-VALUE SERVICES

In 2001, we opened a new Pharmaceutical Development Services (PDS) facility at our site in Swindon, UK. With PDS capabilities in Toronto and Swindon, Patheon can now develop dosage forms for new drug products in both North America and Europe. Products in development generate higher earnings and, if approved, provide opportunities for Patheon to be selected as the commercial manufacturer.



2

MORE EARLY-LIFECYCLE PRODUCTS

In 2001, Patheon was chosen as the commercial manufacturer of five newly launched prescription products for which we had provided development services. Early-lifecycle, patented products create longer revenue streams and hence enhance the profitability of our commercial manufacturing portfolio.



3

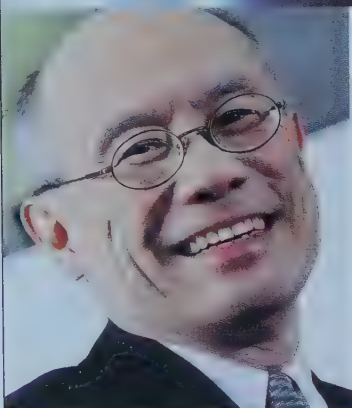
MORE MANUFACTURING CAPACITY

In 2001, Patheon acquired its ninth manufacturing facility. Located in Whitby, Canada and employing more than 400 people, this facility complements the dosage form capabilities of existing sites and adds almost 200,000 square feet to Patheon's capacity. More capacity provides Patheon with the opportunity to manufacture high-volume commercial products.





WE ARE FREQUENTLY
ASKED THE
FOLLOWING
QUESTIONS
BY INVESTORS
AND ANALYSTS



HERE ARE
OUR **ANSWERS**



ROBERT C. TEDFORD
EXECUTIVE VICE-PRESIDENT,
CHEMICALS

WHERE

ALL THE AREAS OF
GREATEST OPPORTUNITY
FOR PATHEON GLOBALLY

WHAT

ARE THE GROWTH PROSPECTS
FOR OUTSOURCING IN TODAY'S
PHARMACEUTICAL INDUSTRY?

The global pharmaceutical market is estimated to be US\$400 billion, of which about US\$80 billion is spent on manufacturing. Within primary manufacturing, about 50% of activity is outsourced. In contrast, only 15% of the \$50 billion secondary manufacturing market – Patheon's segment – is currently outsourced, providing tremendous upside potential for growth.

In addition, the patents on more than 50 of the world's top 100 drugs are due to expire by 2005. Pharmaceutical companies are facing unprecedented pressure to free more

resources for new drug discovery. To do so, they are rationalizing their internal manufacturing networks and implementing alternate supply-chain strategies, including outsourcing. We believe this trend creates excellent growth opportunities for Patheon, which has the financial stability, scope and critical mass to meet the manufacturing needs of the industry's innovators.

Robert C. Tedford
Chief Executive Officer

resources for drug discovery. To do so, they are rationalizing their internal manufacturing networks and implementing alternate supply-chain strategies, including outsourcing. We believe this trend creates excellent growth opportunities for Patheon, which has the financial stability, scope and critical mass to meet the manufacturing needs of the industry's innovators.

There are also significant opportunities to generate additional revenues in both regions with smaller, more specialized pharmaceutical companies and with biotech. Many of these

companies have knowledge and technology that we can leverage and license. They may not have the resources to develop products, but they do have the technology to manufacture. As the largest manufacturer, we can look beyond the North American and European markets to other regions, such as Asia and Latin America, but we will expand only into markets that respect intellectual property rights.

Over the next five years, we will continue to expand our operations in both North America and Europe.



Nick A. DiPietro
PRESIDENT & CHIEF
OPERATING OFFICER

HOW

HAS YOUR COMPANY
MANUFACTURING BUSINESS
EVOLVED IN THE LAST
FEW YEARS?

As our business has shifted toward higher value-added manufacturing, the portfolio of products we manufacture for our clients has grown to include an increasing number of high-profile products. In fiscal 2001, Patheon manufactured 22 of the world's 500 top-selling prescription drugs, compared with only two in 1998. Of these 22 products, nine are still under patent protection, with significant volumes and higher margins.

We are also adding new, early-lifecycle products to our portfolio as a result of our integrated development

and manufacturing services. In fiscal 2001, Patheon was chosen as the commercial manufacturer of five newly launched prescription products for which we had provided development services – up from two in prior years. This is an exciting and significant achievement, demonstrating the ability of our development services business to contribute to longer-stream revenue growth.

Nick A. DiPietro
President & Chief
Operating Officer



Shabbir T. Anik, Ph.D.
EXECUTIVE VICE-PRESIDENT,
PDS & CHIEF SCIENTIFIC OFFICER

WHAT

WERE YOUR ACHIEVEMENTS
IN PHARMACEUTICAL
DEVELOPMENT SERVICES
THIS YEAR?

During the past year, we continued to build our thriving PDS business, expanding our facilities, capabilities and scientific expertise. We invested in additional capacity at Toronto Region Operations with the opening of a new formulation development facility. In addition, we opened a new PDS facility at our site in Swindon, UK, extending our reach to Europe and expanding our development capabilities to include sterile products. Our PDS team grew to include almost 200 skilled staff – including more than 40 Ph.D.s – led by a team of senior managers who each bring an average of 15 years of industry experience to clients' projects.

With this critical mass in place, we were able to work on an increasing number of development projects, covering a broader range of dosage forms and therapeutic categories. At year end, we had 40 products in development on behalf of our clients – a number that compares quite favourably with the late-stage product development pipelines of many of the world's top pharmaceutical companies.

Shabbir T. Anik, Ph.D.
Executive Vice-President,
PDS & Chief
Scientific Officer



ROBERT C. TEDFORD
CHIEF EXECUTIVE OFFICER



ALDO BRACA
EXECUTIVE VICE-PRESIDENT,
EUROPEAN BUSINESS
DEVELOPMENT & PRESIDENT,
PATHEON ITALIA S.p.A.

WHAT

IS NEW ON THE ACQUISITION
HORIZON? ARE YOU LOOKING
FOR MORE COMMERCIAL
MANUFACTURING CAPACITY
OR FACILITIES WITH PDS
CAPABILITIES?

We continue to actively evaluate opportunities to acquire high-quality commercial manufacturing facilities with long-term manufacturing agreements in place. We are also considering acquisitions that expand our PDS capacity or capabilities. However, whether we look at acquisitions that expand our commercial manufacturing or development services, one consideration is paramount: they must meet our strict acquisition criteria, which include quality, an experienced

workforce, flexibility and, in the case of commercial manufacturing facilities, long-term contracts that are accretive to earnings.

Clearly, the United States is an important market for us, and one where we would like to have a physical presence with both commercial manufacturing and product development capabilities. We are also targeting expansion in Western Europe.

Robert C. Tedford
Chief Executive Officer

WHAT

ARE YOU DOING
TO IMPROVE REVENUE
GROWTH IN EUROPE?

Since acquiring our three European sites, we have invested in people, equipment and facilities to transform them into profitable outsourcing units, and have established a sales and marketing infrastructure to market Patheon's name and capabilities throughout Europe. In 2001, we extended our drug development capabilities to Europe with our new PDS facility in Swindon.

While the relatively modest growth of our European revenues in fiscal 2001 was disappointing, it was in no way indicative of the growth opportunities that exist in the European Economic Community. The number of new business enquiries that we are currently pursuing in

Europe almost equals that of North America, and our healthy sales funnel is beginning to bring in new commercial manufacturing and development business at all three sites.

Our capacity and presence in Europe are essential to achieving our vision of global leadership in the pharmaceutical outsourcing sector. We are committed to building on the solid foundation we have established in Europe and are confident that we will achieve better revenue growth rates in 2002.

Aldo Braca
Executive Vice-President,
European Business
Development and
President, Patheon
Italia S.p.A.



SENIOR VICE-PRESIDENT,
FINANCE & TREASURER

WHAT

ARE YOU DOING TO IMPROVE
PATHEON'S EBITDA MARGINS

Looking at our performance over the years, the EBITDA margin has ranged from a low of 7.4% in 1994 to a high of 15.7% in 1999. More recently, our EBITDA margin was 13% in fiscal 2001, which was comparable to fiscal 2000.

We now have a network of nine manufacturing facilities with a broad range of specialized capabilities. This gives us greater operating leverage to enhance our margins as we increase production volumes and improve operational efficiencies throughout our manufacturing network. We also will benefit from

improving the quality of our commercial manufacturing revenue stream as we focus on shifting our mix of business towards early-lifecycle prescription products.

As we have seen throughout our history, our EBITDA margins will fluctuate as we enter into significant long-term manufacturing contracts in connection with the acquisition of sophisticated high-quality manufacturing sites.

Ronald B. Mitchell, C.A.
Senior Vice-President,
Finance & Treasurer



SENIOR VICE-PRESIDENT,
HUMAN RESOURCES,
ENVIRONMENTAL,
HEALTH & SAFETY

HOW

DOES PATHEON ATTRACT
AND RETAIN THE PEOPLE
YOU NEED TO BE SUCCESSFUL?

Since 1997, the size of our workforce has increased fivefold, from just over 500 employees in 1997 to more than 2,500 today.

We aggressively recruit talented individuals globally, attracting candidates with competitive compensation, excellent health and retirement benefits as well as an opportunity to participate in the company-supported, employee share purchase plan. The plan currently is offered to all North American employees and will soon be available to our European employees.

Once employees have joined Patheon, they tend to stay. The turnover rates at all of our facilities are very low, ranging from 2% in Canada to an average of 5% in Europe. We retain

our talent by providing a superior work environment, with exceptional educational and developmental opportunities. In fact, in Canada, we were selected as one of "Canada's Top 100 Employers" by author Richard Yerema in his books of the same name published in 2000 and 2002. Globally in fiscal 2001, more than 450 people – or almost a fifth of our workforce – were transferred or promoted within Patheon, reflecting the talent of our employees as well as our ability to provide a stimulating workplace.

Ron J. Quon
Senior Vice-President,
Human Resources,
Environmental, Health
& Safety

FINANCIAL REVIEW

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Five-Year Financial Summary

(in thousands of Canadian dollars except share information,
per-share amounts and percentages)

	2001 \$	2000 \$	1999 \$	1998 \$	1997 \$
REVENUES AND NET EARNINGS					
Revenues	319,877	256,309	127,395	70,473	50,697
EBITDA (1)	41,433	34,150	20,011	10,370	5,899
(% of revenues)	13.0%	13.3%	15.7%	14.7%	11.6%
Depreciation and amortization	12,685	8,825	5,383	2,297	1,337
Interest	3,009	4,190	2,072	1,561	799
Provision for income taxes	9,418	7,584	5,045	2,530	1,365
Net earnings before unusual items	16,321	13,551	7,357	3,982	2,398
(% of revenues)	5.1%	5.3%	5.8%	5.7%	4.7%
Write-off of after-tax costs of discontinued acquisition	—	—	(402)	—	—
Write down of investment	—	—	—	—	(3,218)
Net earnings (loss)	16,321	13,551	6,955	3,982	(820)
Earnings per share					
Basic	0.34	0.31	0.18	0.12	0.07
Diluted	0.33	0.30	0.17	0.12	0.07
Number of shares					
Outstanding at October 31	50,296	46,121	43,067	34,413	34,302
Weighted average for the year	47,924	43,438	40,382	34,409	34,266
FINANCIAL POSITION					
Current assets	114,039	81,740	62,674	24,022	16,361
Current liabilities	102,236	75,912	43,727	21,235	13,158
Working capital	11,803	5,828	18,947	2,787	3,203
Total assets	353,174	243,242	160,364	64,121	51,104
Interest-bearing debt	51,302	46,540	39,557	22,892	18,186
Shareholders' equity	198,296	124,431	79,223	26,865	22,616
Return on shareholders' equity (4)	10.4%	15.8%	13.9%	16.2%	10.6%
Interest-bearing debt to shareholders' equity	25.9%	37.4%	49.9%	85.2%	80.4%
Interest-bearing debt to total capitalization (5)	20.6%	27.2%	33.3%	46.0%	44.6%
CASH FLOW					
Cash flow from operations (2)	33,068	25,005	11,734	6,485	4,142
Cash provided by operating activities	24,774	11,648	10,815	4,479	2,604
Additions to capital assets					
— sustaining	16,056	11,918	5,480	— (3)	— (3)
— project-related	30,820	16,877	12,921	— (3)	— (3)
Total additions to capital assets	46,876	28,795	18,401	7,653	5,493
Acquisitions	34,900	49,271	13,000	—	14,156
Net proceeds from equity issues	53,915	37,125	45,472	—	12,856
Cash flow from operations per share (2)	0.69	0.58	0.29	0.19	0.12

(1) Earnings before interest, taxes, depreciation and amortization and unusual items

(2) Cash flow from operations before net change in non-cash working capital balances related to operations

(3) Data unavailable for these periods

(4) Ratio of net earnings to the average shareholders' equity during the fiscal year, adjusted for the effect of share proceeds received during the year.

(5) Total capitalization is the sum of interest-bearing debt and shareholders' equity.

Five-Year Summary of Quarterly Results

(in thousands of Canadian dollars except per-share amounts)		Q1	Q2	Q3	Q4	Year
		\$	\$	\$	\$	\$
REVENUES	FY97	9,828	12,640	13,541	14,688	50,697
	FY98	12,715	18,302	17,816	21,640	70,473
	FY99	21,461	34,650	35,228	36,056	127,395
	FY00	50,366	67,886	65,173	72,884	256,309
	FY01	64,216	70,347	86,581	98,733	319,877
EARNINGS BEFORE INTEREST, TAXES, DEPRECIATION AND AMORTIZATION AND UNUSUAL ITEMS (EBITDA)	FY97	1,096	1,437	1,669	1,697	5,899
	FY98	1,523	2,755	2,356	3,736	10,370
	FY99	3,011	5,477	5,471	6,052	20,011
	FY00	5,811	8,223	8,715	11,401	34,150
	FY01	7,861	9,828	9,835	13,909	41,433
EARNINGS BEFORE UNUSUAL ITEMS	FY97	423	615	653	707	2,398
	FY98	487	1,120	878	1,497	3,982
	FY99	1,024	1,847	2,112	2,374	7,357
	FY00	1,783	3,226	3,229	5,313	13,551
	FY01	2,982	3,860	3,635	5,844	16,321
NET EARNINGS	FY97	423	615	653	(2,511) ⁽²⁾	(820)
	FY98	487	1,120	878	1,497	3,982
	FY99	1,024	1,847	1,710 ⁽⁴⁾	2,374	6,955
	FY00	1,783	3,226	3,229	5,313	13,551
	FY01	2,982	3,860	3,635	5,844	16,321
BASIC EPS (CENTS) BEFORE UNUSUAL ITEMS	FY97 ⁽¹⁾	1.2	1.8	1.9	2.1	7.0
	FY98	1.4	3.3	2.5	4.4	11.6
	FY99 ⁽³⁾	2.6	4.6	5.1	5.9	18.2
	FY00 ⁽⁵⁾	4.1	7.5	7.5	12.1	31.2
	FY01 ⁽⁶⁾	6.4	8.3	7.6	11.8	34.1
BASIC EPS (CENTS)	FY97 ⁽¹⁾	1.2	1.8	1.9	(7.3) ⁽²⁾	(2.4)
	FY98	1.4	3.3	2.5	4.4	11.6
	FY99 ⁽³⁾	2.6	4.6	4.1 ⁽⁴⁾	5.9	17.2
	FY00 ⁽⁵⁾	4.1	7.5	7.5	12.1	31.2
	FY01 ⁽⁶⁾	6.4	8.3	7.6	11.8	34.1

(1) FY97 shares issued increased 51% in November 1996 as a result of equity financing.

(2) Includes write down of investment of \$3,218,000 (\$0.094 per share).

(3) FY99 shares outstanding increased 25% as a result of equity offerings in December 1998 and July 1999.

(4) Includes write-off of after-tax costs of discontinued acquisition of \$402,000 (\$0.01 per share).

(5) FY00 shares outstanding increased 7% as a result of an equity offering in October 2000.

(6) FY01 shares outstanding increased 9% as a result of an equity offering in June 2001.

IN FISCAL 2001, PATHEON
SERVED MORE THAN
100 PHARMACEUTICAL
AND BIOTECHNOLOGY
COMPANIES, INCLUDING
15 OF THE WORLD'S
20 LARGEST PHARMA-
CEUTICAL COMPANIES.

Overview

Patheon Inc. ("Patheon" or "the Company") is one of the world's largest independent providers of commercial manufacturing and development services of prescription ("Rx") and over-the-counter ("OTC") drugs to the international pharmaceutical industry. Patheon's vision is to be the pre-eminent provider of pharmaceutical outsourcing services across all dosage forms. The Company owns and operates six manufacturing facilities in and around Toronto, Canada, which comprise 793,000 square feet of capacity, and three manufacturing facilities in Europe: Monza (near Milan), Italy, Swindon, United Kingdom, and Bourgoin-Jallieu (near Lyon), France, which comprise 909,000 square feet of capacity.

Patheon's commercial manufacturing activities relate primarily to Rx and OTC products in solid, semi-solid, liquid and sterile dosage forms. The Company manufactures a wide variety of products in many packaging formats to client specifications. The Company is responsible for each aspect of the manufacturing and packaging process, from sourcing raw materials and packaging components to delivering the finished product in consumer-ready form to the clients' distribution facilities. In most cases, Patheon's clients provide the Company with the active ingredients required for the production of the products. The manufacture of Rx and OTC products accounted for approximately 65% and 24%, respectively, of the Company's revenues in fiscal 2001.

Patheon's pharmaceutical development services ("PDS") include dosage form development, analytical methods development, pilot batch manufacture of new products for the regulatory drug approval process and the provision of scale-up services designed to show that a drug can be manufactured in commercial volumes. Pharmaceutical development services accounted for approximately 11% of the Company's revenues in fiscal 2001.

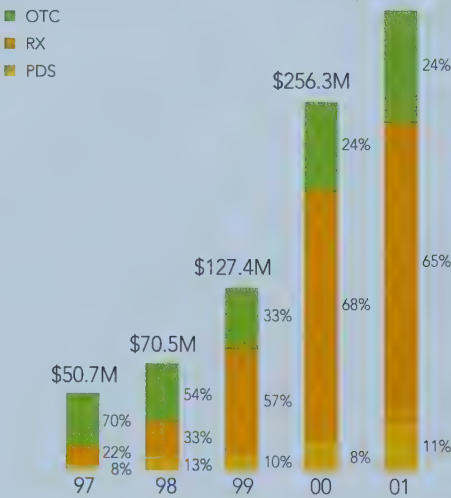
During fiscal 2001, the Company served more than 100 pharmaceutical and biotechnology companies, including 15 of the world's 20 largest multinational pharmaceutical companies.

Consolidated revenues for the year ended October 31, 2001 increased by 25% to \$319.9 million from \$256.3 million in 2000. In fiscal 2001, all service activities contributed to the growth. Commercial manufacturing revenues increased 22%, with Rx up 21% and OTC up 25%. Pharmaceutical development services revenues increased 58% over the previous fiscal year. Strategic growth, principally resulting from new long-term supply agreements with Novartis Pharmaceuticals Canada Inc. and its affiliates, entered into in April 2001, represented 79%, or \$50.4 million of the increase. Net internal growth, or new business from existing sites, was 21%, or \$13.2 million.

During the last five years, the Company's consolidated revenues have grown at an annual compound rate of 58%.

REVENUES BY SERVICE ACTIVITY

(% of total revenues)



Management's Discussion and Analysis of Financial Condition and Results of Operations

Results of Consolidated Operations

Years ended October 31

(in thousands of Canadian dollars, except percentages
and per-share amounts)

	2001 \$	2000 \$	% change
Revenues	319,877	256,309	25%
Operating expenses	278,444	222,159	25%
Earnings before depreciation, amortization, interest and income taxes (EBITDA)	41,433	34,150	21%
(% of revenues)	13.0%	13.3%	—
Depreciation and amortization	12,685	8,825	44%
Interest	3,009	4,190	(28%)
Earnings before income taxes	25,739	21,135	22%
Provision for income taxes	9,418	7,584	24%
Net earnings for the year	16,321	13,551	20%
Earnings per share:			
Basic	\$0.34	\$0.31	10%
Diluted	\$0.33	\$0.30	10%

Quarterly Consolidated Financial Information

(in thousands of Canadian dollars, except per-share amounts)	Revenues \$	EBITDA \$	EBITDA per share		Net earnings \$	Earnings per share	
			Basic \$	Diluted \$		Basic \$	Diluted \$
January 31, 2001	64,216	7,861	0.17	0.16	2,982	0.06	0.06
April 30, 2001	70,347	9,828	0.21	0.20	3,860	0.08	0.08
July 31, 2001	86,581	9,835	0.20	0.20	3,635	0.08	0.07
October 31, 2001	98,733	13,909	0.28	0.27	5,844	0.12	0.12
	319,877	41,433	0.86	0.83	16,321	0.34	0.33
January 31, 2000	50,366	5,811	0.13	0.13	1,783	0.04	0.04
April 30, 2000	67,886	8,223	0.19	0.18	3,226	0.07	0.07
July 31, 2000	65,173	8,715	0.20	0.19	3,229	0.08	0.07
October 31, 2000	72,884	11,401	0.26	0.25	5,313	0.12	0.12
	256,309	34,150	0.78	0.75	13,551	0.31	0.30

The last two quarters of fiscal 2001 include the benefits of the long-term manufacturing and supply agreements with Novartis Pharmaceuticals Canada Inc. and its affiliates, entered into at the time of the purchase of the Whitby, Canada site in April 2001. In the first quarter of fiscal 2001, the underwriters of the October 2000 public offering exercised their over-allotment option and purchased an additional 412,500 common shares. On June 29, 2001, the Company completed a public offering of 3,400,000 common shares. In the 2001 fiscal year, the average number of basic shares outstanding increased by approximately 10% over the 2000 fiscal year and the average number of diluted shares increased by approximately 10% over the prior fiscal year.

Revenues by geographic region and service activity

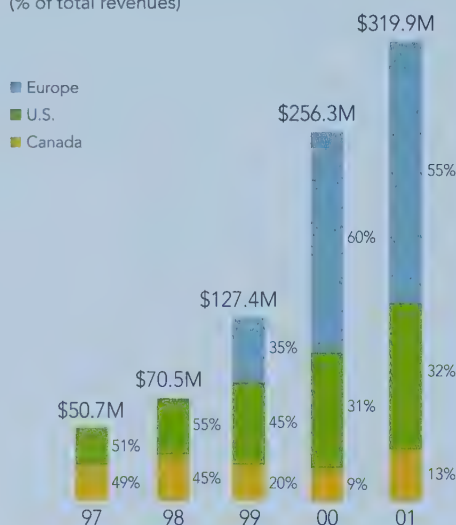
The Company continues to have substantial success in attracting new business for its North American facilities. After reflecting normal declines in existing base business, the net internal growth in North America amounted to \$19,070,000, or 30% of the consolidated growth for the year.

In Europe, the sales and marketing activities are beginning to attract new commercial manufacturing business for all three European sites. However, this new business activity was offset in fiscal 2001 by the decline of existing volumes of mature products and the Company's decision to discontinue a significant OTC contract in the UK because of inadequate pricing. The net result in Europe was a modest

Management's Discussion and Analysis of Financial Condition and Results of Operations

REVENUES BY GEOGRAPHIC REGION

(% of total revenues)



increase of 2% of revenues, although the increase came from an additional month's revenue in fiscal 2001 from the long-term manufacturing and supply agreements entered into at the time of the acquisitions of the France and UK sites at the beginning of December 1999.

In the 2001 fiscal year, commercial manufacturing of prescription drugs and pharmaceutical development services represented 76% of revenue, the same as in 2000. Excluding the impact of the new manufacturing contracts at Whitby, higher-margin prescription manufacturing and pharmaceutical development services represented 79% of revenue, compared with 76% in 2000.

Geographically, revenue growth in North America was \$60.2 million or 59% in 2001. This increase was driven principally by continuing growth in prescription manufacturing and pharmaceutical development service activities, up \$36.4 million or 72% in 2001 over 2000, and the addition of OTC revenues at Whitby.

Revenues by Geographic Region and Service Activity

Years ended October 31

(in thousands of Canadian dollars, except percentages)

	2001 \$	2000 \$	% Change
North America			
Commercial Manufacturing			
Prescription	53,101	28,970	83%
Over-the-counter	75,059	51,273	46%
	128,160	80,243	60%
Pharmaceutical Development Services	33,561	21,284	58%
	161,721	101,527	59%
Europe			
Commercial Manufacturing			
Prescription	155,446	143,922	8%
Over-the-counter	2,633	10,860	(76%)
	158,079	154,782	2%
Pharmaceutical Development Services	77	—	
	158,156	154,782	2%
Total			
Commercial Manufacturing			
Prescription	208,547	172,892	21%
Over-the-counter	77,692	62,133	25%
	286,239	235,025	22%
Pharmaceutical Development Services	33,638	21,284	58%
Consolidated Revenues	319,877	256,309	25%

Management's Discussion and Analysis of Financial Condition and Results of Operations

In Europe, revenues for 2001 were approximately 2% higher than in 2000. Revenues for the 2001 fiscal year include the results of operations for the Swindon and Bourgoin-Jallieu manufacturing sites for twelve months versus eleven months in 2000.

Operating expenses

Operating expenses comprise processing costs, marketing, sales, service, corporate support and administrative expenses. In fiscal 2001, operating expenses increased by 25% over the previous year and, as a percentage of revenues, were comparable with the prior year at approximately 87%. The increase in expenses was the result of higher staffing levels, increased selling, marketing and administrative costs in North America and Europe to support growing business volumes and operating costs of the newly acquired sites in 2001 and 2000.

EBITDA

EBITDA, representing earnings before interest, income taxes, depreciation and amortization, increased by 21% to \$41.4 million in 2001 from \$34.2 million a year earlier. Over the past five years, the Company has achieved a compounded annual growth rate in EBITDA of 63%.

EBITDA margin

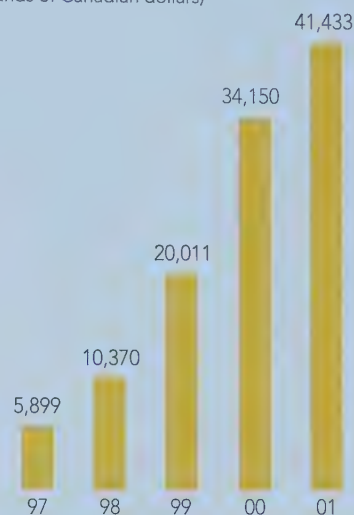
As a percentage of revenues, EBITDA margin was down slightly to 13.0% in 2001 from 13.3% a year earlier. This decrease resulted from a combination of a shift in the service mix in North America, principally related to the addition of lower-margin OTC revenues at Whitby, and the continuing investment by the Company in its management and client services infrastructure in both North America and Europe to position it for further growth.

Depreciation and amortization expenses

Depreciation and amortization expenses of \$12.7 million were \$3.9 million higher than the prior year and represented 4.0% of revenues compared with 3.4% in 2001. The increase was due to the depreciation and amortization expenses recorded as a result of the acquisition of the Whitby site in April 2001 and the acquisition of the remaining interests in Global Pharm Inc. in September 2000. The remainder of the increase was due to the increased capital spending at other sites in North America and Europe.

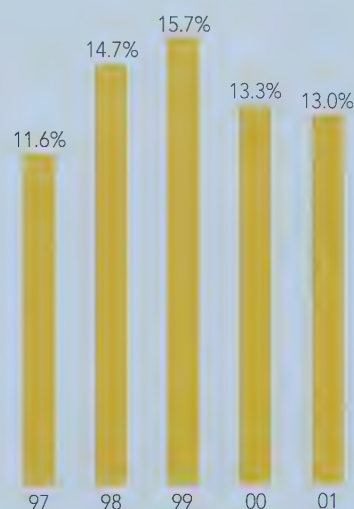
EBITDA

(in thousands of Canadian dollars)



EBITDA MARGIN

(% of revenues)



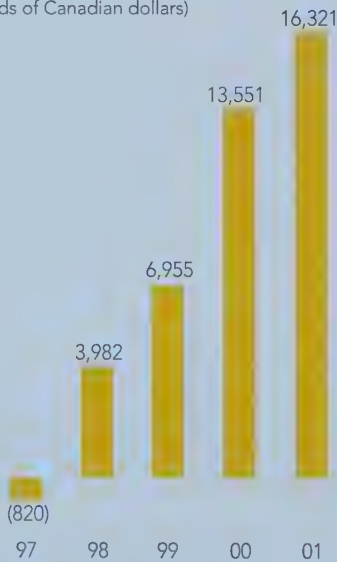
Interest expense

Interest expense of \$3.0 million in 2001 was 28% lower than the \$4.2 million of interest expense in 2000. The higher interest expense in 2000 resulted from both higher interest rates and additional borrowings to finance the acquisitions and working capital requirements of the new European manufacturing facilities. The borrowings were partially repaid towards the end of fiscal 2000 from proceeds of an equity issue by the Company in October 2000. New term financings of approximately \$28 million incurred for the acquisition of the Whitby facility on April 30, 2001 were repaid, along with other term financings in North America, from the proceeds of the equity issue in late June 2001.

NET EARNINGS INCREASED
20% IN 2001. BASIC
EARNINGS PER SHARE
INCREASED 10%, DESPITE
A 10% INCREASE IN
PATHEON'S WEIGHTED
AVERAGE NUMBER OF
SHARES OUTSTANDING.

NET EARNINGS

(in thousands of Canadian dollars)



Earnings before interest, income taxes, depreciation and amortization (EBITDA) were 13.8 times higher than interest expense in 2001, compared with 8.2 times in 2000. Earnings before interest and taxes (EBIT) were 9.6 times higher than interest expense in 2001, compared with 6.0 times in 2000.

The weighted average rate of interest paid on both short- and long-term debt during 2001 was 5.7% compared with 6.6% a year earlier. The reduction in the average interest rate was due to the general easing of global interest rates, particularly in North America, throughout 2001.

The Company benefits from the current favourable interest rate environment. The majority of the Company's lines of credit, other than long-term financing in place at Patheon Italia, are Canadian prime-rate based. During the 2000 fiscal year, the Canadian prime rate increased from 6.25% at the beginning of the year to 7.5% at the end of 2000. At the end of the 2001 fiscal year, the Canadian prime rate had declined to 4.5%.

Earnings before income taxes

Earnings before income taxes increased 22% to \$25.7 million in fiscal 2001 compared with earnings before income taxes of \$21.1 million a year ago.

Income taxes

The consolidated effective income tax rate for the Company in fiscal 2001 was 37% compared with 36% in the previous year. The effective tax rate is dependent on the earnings mix in jurisdictions with differing corporate tax rates. In 2001, a higher portion of consolidated earnings, relating to the York Mills and Whitby operations, was earned in North America, a higher tax jurisdiction in relation to applicable European tax rates.

Net earnings

Net earnings in fiscal 2001 increased by 20% to \$16.3 million compared with \$13.6 million in the previous year. Basic earnings per share were \$0.34 compared with \$0.31 last year – an increase of 10%. Diluted earnings per share were \$0.33 compared with \$0.30 in 2000, an increase of 10%. This was despite an increase in the weighted average number of shares outstanding during 2001 determined on the basic and diluted bases of 10.3% and 9.5%, respectively.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Liquidity and capital structure

For the year ended October 31, 2001, cash generated by operating activities (before net change in non-cash working capital balances related to operations) increased to \$33.1 million (\$0.69 per share) compared with \$25.0 million (\$0.58 per share, as restated) in 2000.

Working capital requirements decreased by \$5.0 million as at the end of the 2001 fiscal year. Cash and cash equivalents decreased by \$2.3 million to \$10.9 million in fiscal 2001. The decrease in cash reflected costs associated with acquiring the new manufacturing site in Whitby and the capital expenditure program in 2001, which were partially offset by proceeds of \$53.9 million from the common share offerings completed during the year. Working capital at October 31, 2001 increased to \$11.8 million from \$5.8 million a year ago, an increase of \$6.0 million. The working capital ratio at October 31, 2001 increased to 1.12:1 from 1.08:1 at October 31, 2000.

Through June 2001, the Company used internal cash and existing available lines with its bankers to finance its capital program. In late June 2001, the Company repaid certain of its term lines in North America using the proceeds of the common share offering referred to above. The Company used cash provided by operating activities and available debt facilities to fund additional capital spending in the balance of the 2001 fiscal year.

Capital expenditures

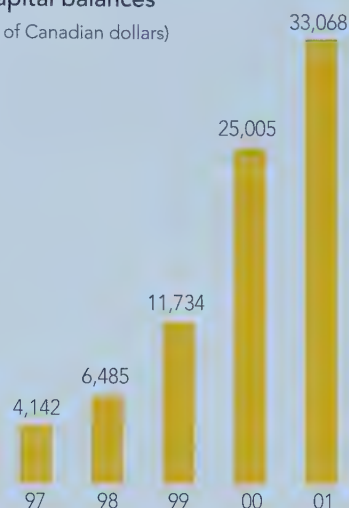
The Company had additions to capital assets of \$46.9 million in 2001 compared with \$28.8 million in 2000. These additions were financed in part from cash provided by operating activities and in part by proceeds of the June, 2001 share offering. The increase in capital expenditures over the prior year reflects higher project-related capital expenditures of approximately \$13.9 million as well as an increase in sustaining capital improvements of approximately \$4.1 million. Project-related expenditures are defined as outlays that will generate growth in capacity and revenues, while sustaining expenditures relate to preservation of existing assets and capacity. At the end of the fiscal year, the Company had major project-related programs underway at its Niagara Region Operations and its Toronto Region Operations in Canada, and at its Swindon, UK and its Monza, Italy facilities in Europe. At October 31, 2001, the Company had commitments of \$11.7 million to complete capital projects under way in North America and Europe.

Interest-bearing and long-term debt

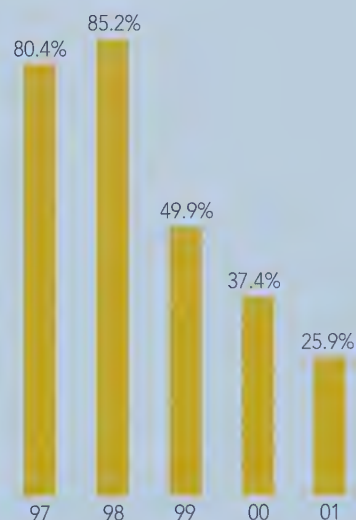
At October 31, 2001, the Company had consolidated interest-bearing debt of \$51.3 million, consisting primarily of \$27.1 million of long-term debt of the Company's Italian subsidiary and \$23.6 million of short-term bank indebtedness.

CASH FLOW FROM OPERATIONS Before net change in non-cash working capital balances

(in thousands of Canadian dollars)



INTEREST-BEARING DEBT TO SHAREHOLDERS' EQUITY



The acquisition of the Whitby site on April 30, 2001 was financed entirely by new debt facilities with the Company's bankers. Approximately \$28 million was drawn under the long-term facilities established with a Canadian bank to finance this acquisition. In June 2001, these long-term debt facilities were repaid through the proceeds of the new equity issue. In addition, certain other term debt facilities in place in Canada were repaid through the proceeds of the equity issue.

Management's Discussion and Analysis of Financial Condition and Results of Operations

In fiscal 2001, the Company's interest-bearing debt-to-equity ratio improved to 25.9% from 37.4% in 2000 and 49.9% in 1999. At October 31, 2001, the Company's consolidated ratio of interest-bearing, long-term debt (including current portion) to shareholders' equity declined to 13.7% compared with 26.1% at October 31, 2000. At October 31, 2001, long-term debt represented 11.1% of invested capital, defined as interest-bearing debt, future tax liabilities and shareholders' equity, compared with 19.6% (as restated) in 2000.

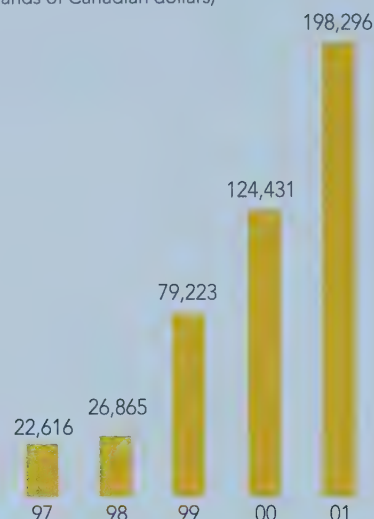
Shareholders' equity

At October 31, 2001, shareholders' equity was \$198.3 million, compared with \$124.4 million at year-end 2000. The increase was the result of net income of \$16.3 million generated in 2001 and net proceeds from equity issues during the year, net of the change in the cumulative translation adjustment account classified in shareholders' equity and the impact of retroactive accounting changes, more fully described in Note 2 of the Company's audited consolidated financial statements for the 2001 fiscal year. In the first quarter of the 2001 fiscal year, the underwriters of the October 2000 public offering exercised their over-allotment option and purchased an additional 412,500 common shares for additional net proceeds of \$5.6 million. On June 29, 2001, the Company completed a public offering of 3,400,000 common shares (including the underwriters' over-allotment option of 400,000 shares) at \$14.65 per share for net proceeds to the Company (after underwriting fees and expenses of the offering) of \$48.3 million. During 2001, the Company issued 362,733 common shares under its stock option plan for proceeds of \$0.2 million.

Exchange gains and losses on translation of the Company's net equity investments in foreign operations are deferred and form the cumulative translation adjustment account, a component of shareholders' equity. Prior to the 2001 fiscal year, the British pound and the euro weakened considerably from the time the Company made its investments in its European businesses. In 2001, these currencies strengthened somewhat resulting in a change in the cumulative translation adjustment account from \$6.4 million at the end of 2000 to \$2.2 million at the end of 2001.

SHAREHOLDERS' EQUITY

(in thousands of Canadian dollars)



Accounting policies

Effective November 1, 2000, the Company adopted the new recommendations of the Canadian Institute of Chartered Accountants ("CICA") with respect to the accounting for income taxes. Although this change had no significant impact on the reported results, the Company has restated its October 31, 2000 balance sheet as a result of this change.

Effective November 1, 2000, the Company adopted, retroactively without restating prior years' results, the new recommendations of the CICA with respect to accounting for employee future benefits. There was no material impact on net earnings for the current fiscal year.

The impact on the balance sheet as at November 1, 2000 as a result of the adoption of these recommendations can be summarized as follows:

Assets:

Future tax assets	\$7.0 million
Capital assets	\$3.5 million

Liabilities and Shareholders' equity:

Future tax liabilities	\$5.1 million
Other long-term liabilities	\$6.1 million
Retained earnings	(\$0.7 million)

Please refer to Note 2 of the Company's audited financial statements for the 2001 fiscal year for additional information on accounting changes.

Management's Discussion and Analysis of Financial Condition and Results of Operations

In June 2001, the Canadian Institute of Chartered Accountants issued new recommendations with respect to Business Combinations and Goodwill and Intangible Assets, effective for fiscal years beginning on or after January 1, 2001, with early adoption permitted in the first quarter for companies with fiscal years commencing on or after April 1, 2001. Under the new recommendations, goodwill and intangible assets deemed to have indefinite lives will no longer be amortized but will be subject to annual impairment tests in accordance with the new recommendations. Other intangible assets will continue to be amortized over their useful lives.

The Company will apply the new recommendations on accounting for goodwill and other intangible assets beginning in its first quarter of 2002. Application of the non-amortization provisions of the new recommendations is expected to result in an increase in pre-tax net income of \$182,000 per year. During 2002, the Company will perform the first of the required impairment tests of goodwill as of October 31, 2002.

In December 2001, the Canadian Institute of Chartered Accountants issued new recommendations with respect to stock-based compensation, effective for fiscal years beginning on or after January 1, 2002. Under the recommendations, companies will be required to account for all issuances of stock or stock options to non-employees in exchange for goods or services, direct awards of stock in exchange for employee services and stock appreciation rights at fair value (using an option pricing model for stock options). Companies will be permitted to account for all other employee stock-based compensation plans using either the fair value approach (which will give rise to compensation expense) or the intrinsic value approach, which will not. The Company does not expect that these new recommendations will have any material impact on its earnings or financial position.

Introduction of the euro

Since January 1, 1999, the euro has been a significant currency for the Company's operations in France and Italy. As of the end of the 2001 fiscal year, the Company has adapted its business processes and information technology systems to handle euro-denominated transactions. The Company's businesses in France and Italy converted to the euro for accounting purposes during 2001.

Environmental, health and safety

The Company has a commitment to safeguard the health of employees and the quality of the environment. Highly qualified environmental, health and safety professionals at all Company locations are dedicated to the maintenance and improvement

of programs and procedures to ensure continued employee and environmental protection. To the best of the Company's knowledge, all of its facilities are in compliance with environmental and occupational health and safety regulations.

Risks and uncertainties

For a more detailed discussion of the risk factors that could materially affect the results of operations and the financial condition of the Company, please refer to the Company's Annual Information Form.

Foreign currency

The Company's foreign exchange exposure continues to increase. In fiscal 2001, approximately 63% of the revenues generated by the Company's North American operations were from clients located in the United States, compared with 74% in 2000 and 69% in 1999. While many contracts are denominated in Canadian dollars, a growing number of contracts are in US dollars. Sourcing arrangements in foreign currencies, primarily US dollars, for raw materials and certain capital expenditures with suppliers outside of Canada act as a natural hedge to partially offset revenues received in US dollars.

In 2001, 49% of the Company's revenues were earned in Europe, compared with 60% in 2000. This is due to the increase in North American revenues arising from the long-term manufacturing contracts related to the acquisition of the Whitby facility in Canada in 2001 and the full-year impact of the acquisition of the remaining interests in Global Pharm Inc. in September 2000. For the first nine months of 2001, the Canadian dollar continued to strengthen against European currencies. In the fourth quarter of 2001, the Canadian dollar weakened against European currencies but not enough to reverse the impact of the first nine months. Had EU exchange rates remained constant at 2000 rates, reported consolidated revenues and net earnings per share for the current year would each have been 1% higher.

As a matter of policy, the Company does not hedge to protect the translated results of its foreign operations. A portion of foreign-denominated cash inflows are naturally hedged by outflows in the same currencies for materials and additions to capital assets as well as payments to service the foreign-denominated debt. Net cash foreign-denominated inflows or outflows are hedged as appropriate to manage risk associated with changes in foreign exchange rates. The Company has controls in place to monitor its foreign exchange exposure.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Interest rates

The Company's current credit arrangements with its Canadian bankers for operations of Patheon Inc., Patheon YM Inc. and Patheon Whitby Inc., include a floating interest rate related to the Canadian prime rate. There is no long-term debt outstanding at the end of the 2001 year with respect to the Company's North American lending arrangements. During 2001, the Company's UK subsidiary negotiated a line of credit with its UK bankers of £7,500,000 (\$17,287,000). The operating line portion bears interest at UK base rate plus 1% and the term line bears interest at the base rate plus 1.5%.

The Company's Italian subsidiary has a line of credit, which bears interest at prime, as well as a mortgage with a floating interest charge linked to Euribor and a mortgage with a fixed interest rate of 4.68%. All of the Italian loans, with the exception of the line of credit, are without recourse to the Company.

The Company is in the process of reviewing its global financing needs with a view to developing more flexible credit facilities.

Acquisitions

On April 30, 2001, the Company completed the purchase from Novartis Pharmaceuticals Canada Inc. of its pharmaceutical manufacturing facility located in Whitby, Canada. Concurrently, the Company entered into long-term manufacturing and supply agreements with Novartis and certain of its affiliates to continue to manufacture substantially all of the products being produced at this facility prior to the acquisition.

The cash consideration of approximately \$34.9 million for the net assets acquired, including the capital assets acquired and related acquisition costs and inventories less liabilities assumed, was financed through new short and long-term debt facilities with one of the Company's Canadian bankers. Interest rates were tied to prime. The long-term debt facilities used to finance the acquisition were repaid in full with the proceeds of the equity issue of June 29, 2001.

On September 1, 2000, Patheon acquired the remaining 52% of Global Pharm Inc. (Patheon YM Inc., now operating as Toronto York Mills Operations), representing all the shares that it did not already own. The total cash consideration, including the capitalization of acquisition costs, less liabilities assumed, was \$10.4 million. The acquisition was financed by a new line of credit with a bank with which the Company had not previously had a banking relationship. A portion of the proceeds of the Company's public offering of shares on October 6, 2000 was used to repay this bank line.

Outlooks and markets

At October 31, 2001, orders for delivery in the first quarter, on a company-wide basis, amounted to approximately \$95 million, or 48% higher than a year ago. Despite the current difficult economic climate, the Company is experiencing an increase in new business enquiries. The Company is pleased with the increasing activity in the European market and the continuing growth of the pharmaceutical development business. At October 31, 2001, there were 40 products under development on behalf of clients, of which 11 were in Phase III and 5 were awaiting NDA approval. The Company expects that it will be providing commercial manufacturing services for these products if they receive NDA approval.

The Company receives updated forecasts of production service requirements from its existing clients regularly. Based on these current forecasts and based on the Company's current expectations of new revenue opportunities, revenues in 2002 are expected to approach \$400 million and margins are expected to be comparable with those in 2001.

The Company continues to investigate the acquisition of additional high-quality manufacturing sites. Acquiring facilities in the USA is important to the Company's strategy, and efforts are accelerating in this regard. The Company will also seriously consider acquiring sites in Europe to build on its existing high-quality manufacturing network. Patheon's strategy is to serve the industry innovators – those companies focused on new drug development – and to improve the quality of its revenue stream. The Company's strong and consistent results over the years demonstrate that its strategy is sound.

Forward-looking information

Certain statements in this report may constitute forward-looking statements. Such forward-looking statements involve risks, uncertainties and other factors, which may cause actual results, performance or achievements of the Company to be materially different from future results, performance or achievements expressed or implied by such forward-looking statements.

Auditors' Report

To the Shareholders of Patheon Inc.

We have audited the consolidated balance sheets of **Patheon Inc.** as at October 31, 2001 and 2000 and the consolidated statements of earnings, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at October 31, 2001 and 2000 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Toronto, Canada
December 10, 2001.

Ernst & Young LLP

Chartered Accountants

Consolidated Balance Sheets

As at October 31 (in thousands of Canadian dollars)	2001 \$	2000 \$ <i>(restated-note 2)</i>
ASSETS		
Current		
Cash and cash equivalents <i>(note 4)</i>	10,916	13,236
Accounts receivable	65,563	42,192
Inventories <i>(note 5)</i>	37,560	26,312
Total current assets	114,039	81,740
Capital assets, net <i>(note 6)</i>	226,048	151,488
Future tax assets <i>(note 12)</i>	7,754	5,116
Goodwill <i>(note 3)</i>	3,456	3,638
Investment	1,877	1,260
	353,174	243,242
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Bank indebtedness	23,590	13,155
Accounts payable and accrued liabilities	70,214	51,642
Income taxes payable	2,286	2,196
Current portion of long-term debt <i>(note 7)</i>	6,146	8,919
Total current liabilities	102,236	75,912
Long-term debt <i>(note 7)</i>	21,234	28,455
Other long-term liabilities <i>(note 8)</i>	19,196	9,274
Future tax liabilities <i>(note 12)</i>	12,212	5,170
Total liabilities	154,878	118,811
Shareholders' equity		
Share capital <i>(note 10)</i>	154,830	100,737
Retained earnings	45,710	30,052
Cumulative translation adjustment <i>(note 9)</i>	(2,244)	(6,358)
Total shareholders' equity	198,296	124,431
	353,174	243,242

See accompanying notes

On behalf of the Board:



PETER A. W. GREEN
DIRECTOR



ROBERT C. TEDFORD
DIRECTOR

Consolidated Statements of Earnings

Years ended October 31 (in thousands of Canadian dollars except earnings per share)	2001 \$	2000 \$
Revenues	319,877	256,309
Operating expenses	278,444	222,159
Earnings before depreciation and amortization, interest and income taxes	41,433	34,150
Depreciation and amortization	12,685	8,825
Interest (note 7)	3,009	4,190
Earnings before income taxes	25,739	21,135
Provision for income taxes (note 12)		
Current	5,024	5,708
Future	4,394	1,876
	9,418	7,584
Net earnings for the year	16,321	13,551
Earnings per share (note 9)		
Basic	\$0.34	\$0.31
Diluted	\$0.33	\$0.30

See accompanying notes

Consolidated Statements of Retained Earnings

Years ended October 31 (in thousands of Canadian dollars)	2001 \$	2000 \$
Retained earnings, beginning of year	30,052	16,501
Accounting change (note 2)	(663)	—
Net earnings for the year	16,321	13,551
Retained earnings, end of year	45,710	30,052

See accompanying notes

Consolidated Statements of Cash Flows

Years ended October 31 (in thousands of Canadian dollars)	2001 \$	2000 \$
OPERATING ACTIVITIES		
Net earnings for the year	16,321	13,551
Add (deduct) charges to operations not requiring a current cash payment		
Depreciation and amortization	12,685	8,825
Employee future benefits	(332)	753
Future income taxes	4,394	1,876
Cash provided from operations	33,068	25,005
Net change in non-cash working capital balances related to operations	(8,294)	(13,357)
Cash provided by operating activities	24,774	11,648
INVESTING ACTIVITIES		
Acquisition of new manufacturing sites <i>(note 3)</i>		
Capital and other assets acquired	(37,100)	(56,643)
Liabilities assumed	2,200	7,372
Cash consideration	(34,900)	(49,271)
Additions to capital assets		
Sustaining	(16,056)	(11,918)
Project-related	(30,820)	(16,877)
Total additions to capital assets	(46,876)	(28,795)
Increase in investment	(617)	—
Cash used in investing activities	(82,393)	(78,066)
FINANCING ACTIVITIES		
Increase in bank indebtedness	10,244	3,611
Increase in term loans	44,636	38,505
Repayment of long-term debt and other long-term liabilities	(57,169)	(31,284)
Issue of common shares	54,093	37,405
Cash provided by financing activities	51,804	48,237
Effect of exchange rate changes on cash and cash equivalents	3,495	7,072
Net decrease in cash and cash equivalents during the year	(2,320)	(11,109)
Cash and cash equivalents, beginning of year	13,236	24,345
Cash and cash equivalents, end of year	10,916	13,236
Supplemental cash flow information		
Interest paid	3,417	4,784
Income taxes paid	3,455	10,612
See accompanying notes		

Notes to Consolidated Financial Statements

October 31, 2001 and 2000

(dollar information in tabular form is expressed in thousands of Canadian dollars)

1. Basis of presentation and summary of significant accounting policies

Patheon Inc. ("Patheon" or the "Company") is a Canadian public company, which trades under the symbol PTI on The Toronto Stock Exchange. The Company is an independent provider of commercial manufacturing and development services of prescription ("Rx") and over-the-counter ("OTC") drugs to the international pharmaceutical industry.

Patheon's commercial manufacturing activities relate primarily to Rx and OTC products in solid, semi-solid, liquid and sterile dosage forms. The Company manufactures to client specifications a wide variety of products in many packaging formats. The Company is responsible for each aspect of the manufacturing and packaging process, from sourcing raw materials and packaging components to delivering the finished product in consumer-ready form to the client's distribution facilities.

Patheon's pharmaceutical development services include dosage form development, analytical methods development, pilot batch manufacture of new products for the regulatory drug approval process and the provision of scale-up services designed to show that a drug can be manufactured in commercial volumes.

The consolidated financial statements of the Company have been prepared by management in accordance with Canadian generally accepted accounting principles. The significant accounting policies followed by the Company are summarized as follows:

Principles of consolidation

These consolidated financial statements include the accounts of the Company and its subsidiaries. Prior to September 1, 2000, the results of Global Pharm Inc., a corporate joint venture, were proportionately consolidated with those of the Company (note 3). All significant intercompany transactions have been eliminated.

Revenue recognition

The Company recognizes revenue when services are completed in accordance with the specific terms of contractual arrangements with its clients and all costs connected with providing these services have been incurred.

Foreign exchange translation

Monetary assets and liabilities of the Company denominated in foreign currencies are translated at the year-end exchange rates. Exchange gains and losses on revenues and expenses are recognized in earnings in the current period.

The Company's operations outside of Canada are considered self-sustaining and accordingly their accounts are translated to Canadian dollars using the year-end exchange rates, and revenues and expenses are translated at average rates during the year. Exchange gains or losses on translation of the Company's net equity investment in these operations are deferred as a separate component of shareholders' equity.

The appropriate amounts of exchange gains or losses accumulated in the separate component of shareholders' equity are reflected in earnings when there is a reduction in the Company's net investment in the operations that gave rise to such exchange gains and losses.

Cash and cash equivalents

Cash and cash equivalents include cash in interest-bearing accounts and term deposits with remaining maturities of less than three months at the date the term deposit was acquired.

Inventories

Inventories consisting of raw materials, packaging components and work-in-process are valued at the lower of weighted average cost and net realizable value.

Capital assets

Capital assets are carried at cost less accumulated depreciation. The cost of assets disposed of and the related accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in earnings.

1. Basis of presentation and summary of significant accounting policies *(continued)*

Depreciation is provided on the straight-line basis based on estimated useful lives as follows:

Buildings	40-50 years
Machinery and equipment	5-15 years
Office equipment	4-10 years
Furniture and fixtures	10 years

Repairs and maintenance costs are charged to operations as incurred.

In the consolidated statements of cash flows, additions to capital assets are classified as either project-related (additions related to revenue growth) or sustaining (additions related to the preservation of existing facilities).

Goodwill

Goodwill represents the excess of the purchase price of the Company's interest in subsidiary companies over the fair value of the underlying net identifiable assets arising on acquisitions. Goodwill is being amortized to earnings on a straight-line basis over 20 years. On an ongoing basis, management reviews the valuation and amortization periods of goodwill whenever events or changes in circumstances warrant such a review. In doing so, the Company evaluates whether there has been a permanent impairment in the value of unamortized goodwill based on the estimated undiscounted cash flows of each business to which the goodwill relates.

Investment

The investment in the shares of a development stage drug technology company is accounted for on the cost basis whereby the Company records, as earnings, its share of dividends as declared. On an ongoing basis, management reviews the valuation of the investment, taking into consideration any events or circumstances which might have impaired its carrying value.

Employee benefit plans

The cost of pension and post-employment benefits related to employees' current service is charged to earnings annually. The cost is computed on an actuarial basis using the projected benefit method prorated on service and management's best estimates of investment yields, salary escalation and other factors. Pension plan assets are valued at fair value for purposes of calculating the expected return on plan assets. Past service costs resulting from plan amendments are amortized over the remaining service life of active employees. The excess of the net actuarial gain or loss over 10% of the greater of the benefit obligations and the fair value of plan assets is amortized over the average remaining service period of active employees.

Unfunded termination benefits for the Company's Italian employees are accrued based on Italian severance pay statutes. The liability recorded on the consolidated balance sheet is the amount to which the employees would be entitled if the employees separated immediately. Unfunded retirement indemnities for the Company's French employees are calculated by an actuarial valuation in accordance with French civil and labour laws.

Income taxes

The Company follows the liability method of income tax allocation. Under this method, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the substantially enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Share-based compensation plan

The Company has an incentive stock option plan as more fully described in note 10. No compensation expense is recognized for this plan when stock or stock options are issued. Any consideration paid on the exercise of stock options is credited to share capital.

Earnings per share

The calculation of earnings per common share is based on the reported net earnings divided by the weighted average number of shares outstanding during the year. Diluted earnings per share reflect the assumed conversion of all diluted securities using the treasury stock method.

2. Accounting changes

Income taxes

Effective November 1, 2000, the Company adopted, retroactively with restatement of prior years, the new recommendations of The Canadian Institute of Chartered Accountants ("CICA") with respect to accounting for income taxes. Under the new liability method, future income tax assets and liabilities are determined based on reporting differences between the basis of assets and liabilities used for financial statement and income tax purposes. Such differences are then measured using substantially enacted tax rates and laws that will be in effect when these differences are expected to reverse.

Prior to the adoption of the new recommendations, income tax expense was determined using the deferral method of tax allocation. Under this method, future tax expense was based on items in income and expense that were reported in different years in the financial statements and tax returns and measured at the tax rate in effect in the year the difference originated.

As a result of this change, future income tax assets and liabilities as at October 31, 2000 increased by \$5,116,000. This change had no impact on reported results for 2000 or 2001.

Employee future benefits

Effective November 1, 2000, the Company adopted, retroactively without restating prior years' results, the new recommendations of the CICA for accounting for employee future benefits. Under the new recommendations, the Company's projected benefit obligation is discounted using a market-related discount rate. Previously, the discount rate used was based on management's best estimate of long-term rates.

In addition, the Company provides post-retirement benefits other than pensions. The new recommendations require that these costs, based on the terms of the plan, be recognized on an accrual basis during the years the plan participants provide the services. Previously, the cost of providing these benefits was expensed when paid.

The result was to increase employee future benefits by \$6,063,000, increase future tax assets by \$1,900,000, increase capital assets by \$3,500,000, and decrease retained earnings by \$663,000.

Earnings per common share

Effective January 1, 2001, the Company retroactively adopted the new recommendations of the CICA with respect to the computation of diluted earnings per common share. Under the new standard, the treasury stock method is used in determining the dilutive effect of warrants and options. Previously, the inputed earnings approach was used. As a result of this change, previously reported diluted earnings per share decreased from \$0.31 to \$0.30.

3. Acquisitions of new manufacturing sites

- (a) On April 30, 2001, the Company acquired a pharmaceutical manufacturing facility located in Whitby, Canada, for total cash consideration of \$34,900,000, including related acquisition costs.

The acquisition has been accounted for using the purchase method and the accompanying consolidated financial statements include the results of operations from the date of purchase.

The purchase price was allocated in the accounts based on the estimated fair value of the assets acquired less liabilities assumed as follows:

	\$
Capital and other assets acquired	29,900
Inventory acquired	7,200
Other long-term liabilities assumed	(2,200)
Cash consideration for net assets acquired	34,900

- (b) On December 1, 1999, the Company completed the acquisition of two pharmaceutical manufacturing facilities located in Swindon, UK and Bourgoin-Jallieu, France for total cash consideration of \$38,871,000 including capitalized acquisition costs. These acquisitions were accounted for using the purchase method and the accompanying consolidated financial statements include the results of operations from the date of purchase.

Notes to Consolidated Financial Statements

ns of new manufacturing sites (continued)

The purchase price was allocated in the accounts based on the estimated fair value of the assets acquired less liabilities assumed as follows:

	\$
Capital and other assets acquired	41,213
Future tax asset	2,038
Other liabilities	(4,380)
Cash consideration for net assets acquired	38,871

- (c) On September 1, 2000, the Company acquired 52% of the shares of Global Pharm Inc., representing all of the shares the Company did not previously own. The total cash consideration for the share purchase was \$10,400,000 including capitalized acquisition costs. Subsequent to the acquisition, Global Pharm Inc. was renamed Patheon YM Inc. and operates as Toronto York Mills Operations. The acquisition has been accounted for using the purchase method and the accompanying consolidated financial statements include the results of operations from the date of purchase.

The purchase price was allocated in the accounts based on the estimated fair value of the assets acquired less liabilities assumed as follows:

	\$
Capital and other assets acquired	11,933
Goodwill	3,653
Liabilities assumed	
Net current liabilities	(2,194)
Long-term debt	(2,992)
Cash consideration for net assets acquired	10,400

Cash and cash equivalents

	2001 \$	2000 \$
Interest-bearing balances with banks	1,758	3,338
Term deposits	9,158	9,898
	10,916	13,236

	2001 \$	2000 \$
Raw materials and packaging	24,284	17,284
Work-in-process	13,276	9,028
	37,560	26,312

Notes to Consolidated Financial Statements

6. Capital assets

	2001			2000
	Cost \$	Accumulated depreciation \$	Net book value \$	Net book value \$
Land	18,732	—	18,732	15,971
Buildings	91,964	8,596	83,368	57,560
Machinery and equipment	114,452	27,081	87,371	61,807
Office equipment	9,052	4,789	4,263	4,416
Furniture and fixtures	6,249	4,347	1,902	1,994
Construction in progress and deferred costs	30,412	—	30,412	9,740
	270,861	44,813	226,048	151,488

Capital commitments to complete authorized capital projects were \$11,700,000. The majority of these expenditures are expected to be incurred during the year ending October 31, 2002.

7. Long-term debt

	2001 \$	2000 \$
Term loans bearing interest at prime plus 1/2%	—	2,250
Subordinated mortgage, bearing interest at prime	1,500	1,500
Non-interest bearing note	—	4,441
Other	298	443
	1,798	8,634
Debt of subsidiaries without recourse to the Company		
Mortgage, bearing interest at prime plus 3.25% per annum	—	5,325
Mortgage, bearing interest at 4.68% per annum (Euros 13,705,000)	19,552	18,732
Mortgage, bearing interest at Euribor plus 0.7% (Euros 4,226,000)	6,030	4,683
	25,582	28,740
	27,380	37,374
Less current portion	6,146	8,919
	21,234	28,455

The Company has a line of credit with its Canadian bankers of \$30,000,000. The operating line portion, with interest at prime, may not exceed the lesser of \$15,000,000 and the total of an allowable portion of accounts receivable and inventory. The demand revolving-loan portion, which is not to exceed \$15,000,000, bears interest at the minimum rate of prime plus 1/2% or the maximum rate of prime plus 1%. The line of credit is collateralized by a general security agreement and fixed and floating charge debentures covering all of the Company's Canadian assets, other than the shares of its wholly owned subsidiaries, Patheon YM Inc. and Patheon Whitby Inc. As at October 31, 2001, the line of credit utilized by the Company amounted to \$12,365,000 (2000 - \$15,405,000). The Company is in the process of renegotiating the line of credit by January 31, 2002.

Patheon YM Inc., a wholly owned subsidiary of the Company, has a line of credit with its Canadian bankers of \$13,000,000. The operating line portion, with interest at prime, may not exceed the lesser of \$6,000,000 and the total of an allowable portion of accounts receivable and inventory. The demand reducing-loan portion, which is not to exceed \$7,000,000, bears interest at prime plus 1/2%. The line of credit is collateralized by general security agreements and fixed and floating charge debentures covering the assets of the borrower, a pledge of shares of the borrower and guarantees by the Company and certain of its subsidiaries. As at October 31, 2001, the line of credit utilized by the Company amounted to \$1,938,000.

7. Long-term debt (continued)

Patheon Whitby Inc., a wholly owned subsidiary of the Company, has a line of credit with its Canadian bankers of \$40,000,000. The operating line portion, with interest at prime, may not exceed the lesser of \$10,000,000 and the total of an allowable portion of accounts receivable and inventory. The demand reducing-loan portion, which is not to exceed \$30,000,000, bears interest at rates of prime plus 1/2% to prime plus 3/4%. The line of credit is collateralized by general security agreements and fixed and floating charge debentures covering the assets of the borrower, a pledge of shares of the borrower and guarantees by the Company and certain of its subsidiaries. As at October 31, 2001, the line of credit utilized by the Company amounted to \$4,650,000.

The Company's UK subsidiary has a line of credit with its UK bankers of £7,500,000 (\$17,287,000). The operating line portion, with interest at base rate plus 1%, may not exceed the lesser of £3,000,000 (\$6,915,000) and an allowable portion of accounts receivable. The unused term line of £4,500,000 (\$10,372,000) would, if drawn, bear interest at the base rate plus 1.5%. The line of credit is collateralized by general security agreements and fixed and floating charge debentures covering the assets of the borrower, a pledge of shares of the borrower and guarantees by the Company and certain of its subsidiaries. As at October 31, 2001, the line of credit utilized by the Company amounted to £1,639,000 (\$3,772,000).

The Company's Italian subsidiary has lines of credit with its European banker of euros 1,032,000 (\$1,472,000), which, if drawn, would bear interest at a rate of 8% to 8.25%. The Company also has a line to discount invoices of euros 2,582,000 (\$3,684,000) which, if drawn, would bear interest at 5.25%.

The subordinated mortgage bears interest at prime, payable semi-annually, with principal due on January 31, 2002.

The mortgage bearing interest at 4.68%, assumed on the acquisition of Patheon Italia S.p.A., is non-recourse to the Company and is collateralized by a first mortgage on the Italian subsidiary's building. The mortgage is repayable in equal semi-annual amounts until December 31, 2008.

The mortgage bearing interest at Euribor plus 0.7%, assumed on the acquisition of Patheon Italia S.p.A., is also non-recourse to the Company and is collateralized by a second mortgage on the Italian subsidiary's building. Principal repayments commenced on March 31, 2001 and are payable in equal semi-annual amounts until March 31, 2006.

The estimated fair market value of the Company's long-term debt approximates its carrying value.

The estimated minimum annual repayment schedule for long-term debt based on current exchange rates is: 2002 - \$6,146,000; 2003 - \$3,790,000; 2004 - \$3,856,000; 2005 - \$3,944,000; 2006 - \$3,286,000.

Interest on long-term debt amounted to \$2,140,000 (2000 - \$3,905,000) for the year.

8. Other long-term liabilities

	2001 \$	2000 \$
Unfunded termination indemnities (EUR 3,900,000)	5,594	4,717
Unfunded retirement indemnities (EUR 3,400,000)	4,884	4,105
Employee future benefits (note 13)	8,386	—
Preferred shares (note 10)	452	572
	19,316	9,394
Less current portion included in accounts payable and accrued liabilities	120	120
	19,196	9,274

8. Other long-term liabilities (continued)

The unfunded termination indemnities relate to the employees of the Company's Italian subsidiary. In accordance with Italian severance pay statutes, an employee benefit is accrued for service to date and is payable immediately upon separation from employment. The termination indemnity liability is calculated in accordance with local civil and labour laws based on each employee's length of service, employment category and remuneration. The termination liability is adjusted annually by a cost-of-living index provided by the Italian Government. There is no vesting period or funding requirement associated with the liability. The liability recorded in the consolidated balance sheet is the amount to which the employees would be entitled if the employees separated immediately. The expense for the year amounted to \$854,000 (2000 - \$1,044,000).

The unfunded retirement indemnities relate to the employees of the Company's French subsidiary. The liability is calculated by an actuarial valuation in accordance with French civil and labour laws. A lump sum payment is made to employees on their retirement date. The amount expensed for the year amounted to \$362,000 (2000 - \$300,000).

9. Other information*Corporate joint venture*

The Company's share of operations of its corporate joint venture for the period from November 1, 1999 to August 31, 2000 is as follows:

	2000 \$
Revenues	6,327
Other expenses	6,388
Depreciation	338
Interest on long-term debt	221
Net loss	(368)
Cash used in operating activities	(225)
Cash used in investing activities	(443)
Cash used in financing activities	(100)

Cumulative translation adjustment

Unrealized translation adjustments, which arise on the translation to Canadian dollars of assets and liabilities of the Company's self-sustaining foreign operations, resulted in an unrealized currency translation gain of \$4,114,000 for the year ended October 31, 2001. The unrealized gain resulted primarily from the strengthening of the euro and the British pound against the Canadian dollar.

Earnings per share

The following is a reconciliation of the numerator and denominator of earnings per share computations:

	2001	2000
Net earnings for the year	\$16,321	\$13,551
Weighted average shares outstanding (numbers in thousands)	47,924	43,438
Effect of dilutive stock options	1,650	1,817
Diluted weighted average shares outstanding	49,574	45,255
Earnings per share		
Basic	\$0.34	\$0.31
Diluted	\$0.33	\$0.30

Options to purchase 706,466 and 112,500 common shares for the years ended October 31, 2001 and 2000, respectively, were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of the common shares.

Notes to Consolidated Financial Statements

Share capital

Share capital consists of the following:

	2001 \$	2000 \$
Authorized		
Unlimited Class I preferred shares issuable in series, eligible for a cumulative cash dividend of \$6.00 per share payable annually in arrears. Redeemable at the option of the Company for \$100 with 1,331 shares being required to be redeemed annually		
Unlimited common shares		
Issued and outstanding		
5,022 Class I preferred shares, Series A (2000 - 6,353)	452	572
50,295,925 common shares (2000 - 46,120,692)	154,830	100,737

Preferred shares

Due to their mandatory redemption provisions, the Company's preferred shares are classified as other long-term liabilities and associated dividends paid are reflected as interest expense. During each of 2001 and 2000, the Company redeemed 1,331 of its preferred shares at \$100 per share.

Shares issued

During the year, the Company completed a public offering and issued 3,400,000 common shares for net after-tax proceeds of \$48,333,000 (2000 - 2,750,000 common shares for net proceeds of \$37,125,000). In addition, the Company issued 362,733 (2000 - 303,565) common shares under the stock option plan for proceeds of \$178,000 (2000 - \$280,000).

During the year, the underwriters of the public offering in October 2000 exercised their over-allotment option and purchased an additional 412,500 common shares for net after tax proceeds of \$5,582,000.

Incentive stock option plan

The Company has an incentive stock option plan, which provides for the granting of options for the benefit of employees, officers and directors. The total number of Company shares that may be issued under this plan is 4,622,692. The exercise price per share will be the market price at the time of granting and the maximum term is 10 years. Options generally vest equally after the end of the first, second and third year of grant; however, under certain circumstances, options vest immediately.

A summary of the plan and changes during each of 2001 and 2000 are as follows:

	2001		2000	
	Shares #	Weighted average exercise price \$	Shares #	Weighted average exercise price \$
Outstanding, beginning of year	2,836,368	3.78	2,429,600	2.03
Granted	754,800	15.10	725,000	8.43
Exercised/forfeited	(395,169)	1.56	(318,232)	0.95
Outstanding, end of year	3,195,999	6.73	2,836,368	3.78
Options exercisable at year end	2,104,614	3.80	1,775,357	1.89

The following table summarizes information about options outstanding at October 31, 2001:

Range of exercise prices	Options outstanding			Options exercisable	
	Number outstanding	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable	Weighted average exercise price
\$0.29-1.66	970,800	3.7 years	\$1.06	970,800	\$1.06
\$2.40-3.53	636,668	4.4 years	\$3.02	516,660	\$2.91
\$8.15-15.80	1,588,531	8.5 years	\$11.69	617,154	\$8.84

11. Shareholder rights plan

On March 23, 1999, the shareholders approved a shareholder rights plan (the "Plan"). The Plan applies to all common shares and all future issues of common shares. The Plan is designed to encourage fair treatment of all the Company's shareholders in the event of a take-over bid, to provide shareholders and the Board of Directors with more time to fully consider any unsolicited take-over bid for the Company, to allow the Board of Directors more time to pursue other alternatives to maximize shareholder value, if appropriate, and to prevent creeping or coercive take-over bids. The Plan will be in effect until the close of the 2002 shareholders' meeting of the Company.

Under the terms of the Plan, one right has been granted for each common share. Each right entitles the registered holder to purchase an additional common share for \$7 but is not exercisable until certain events occur. The rights issued under the Plan become exercisable only when a person, including any party related to it, acquires or announces its intention to acquire 20% or more of the Company's outstanding common shares without complying with the "Permitted Bid" provisions or without approval of the Board of Directors. Should such an acquisition occur, each right would entitle a holder, other than the acquiring person and persons related to it, to purchase common shares of the Company at a 50% discount to the market price.

A Permitted Bid is a bid made to all shareholders that is open for at least 60 days. If at the end of 60 days at least 50% of the outstanding shares, other than those owned by the offeror and certain related parties, have been tendered, the offeror may take up and pay for the shares but must extend the bid for a further 10 days to allow other shareholders to tender. This will provide shareholders with more time to consider the bid and any other options that may be available. The Board of Directors will also have more time to consider alternatives and to make recommendations to shareholders.

12. Income taxes

The following is a reconciliation of the expected income tax expense obtained by applying the combined corporate tax rates to income before income taxes:

	2001 \$	2000 \$
Expected income tax expense using statutory tax rates	8,805	7,422
Permanent differences and other		
Foreign	421	672
Domestic	326	14
Foreign rate differentials	(134)	(524)
Provision for income taxes	9,418	7,584
Effective tax rate	36.6%	35.9%

Components of future income taxes by jurisdiction are summarized as follows:

	2001 \$	2000 \$
Canada		
Future income tax assets – long-term		
Share issue costs	1,386	1,289
Accounting provisions not currently deductible for tax purposes	591	194
	1,977	1,483
Future income tax liabilities – long-term		
Tax depreciation in excess of book depreciation	6,597	3,640
Other	111	—
	6,708	3,640
Foreign		
Future income tax assets – long-term		
Accounting provisions not currently deductible for tax purposes	5,041	3,236
Other	736	397
	5,777	3,633
Future income tax liabilities – long term		
Tax depreciation in excess of book depreciation	5,311	1,530
Other	193	—
	5,504	1,530

13. Employee future benefits

The Company has a number of defined benefit and defined contribution plans providing pension, other retirement and post-employment benefits to substantially all of its employees.

Information about the Company's defined benefit plans, in aggregate, is as follows:

	Pension 2001 \$	Other benefit plans 2001 \$
Change in benefit obligation		
Benefit obligation, beginning of year	46,603	3,233
Current service cost	1,775	378
Interest cost	1,997	179
Benefits paid	—	(15)
Actuarial loss	—	215
Actuarial obligation, end of year	50,375	3,990
Change in plan assets		
Market value of plan assets, beginning of year	44,828	—
Actual return of plan assets	(4,882)	—
Member contributions during the year	444	—
Employer contributions	1,775	15
Benefits paid	—	(15)
Actual plan expenses	(444)	—
Market value of plan assets, end of year	41,721	—
Reconciliation of funded status		
Funded status, deficit	(8,654)	(3,990)
Member contributions after measurement date	666	—
Unamortized net actuarial loss	3,379	213
Accrued benefit liability	(4,609)	(3,777)

The accrued benefit liabilities are included in other long-term liabilities (note 8).

The significant actuarial assumptions adopted in measuring the Company's accrued benefit obligations are as follows (weighted-average assumptions as of October 31):

	Pension 2001 %	Other benefit plans 2001 %
Discount rate	6	7
Expected long-term rate of return on plan assets	7	—
Rate of compensation increase	4.25	—

For measurement purposes, a 4% to 11% annual rate of increase in the per capita cost of covered health care and dental benefits was assumed for 2001. The rate was assumed to decrease gradually over the next six years to 4% to 6% and remain at that level thereafter.

Notes to Consolidated Financial Statements

13. Employee future benefits (continued)

The Company's net benefit plan expense is as follows:

	Pension 2001 \$	Other benefit plans 2001 \$
Components of defined benefit plan expense		
Current service cost	1,775	378
Interest cost	1,997	179
Expected return on plan assets (income)	(2,497)	—
Net expense	1,275	557

Effective May 1999, the Company has provided retirement benefits for the majority of its Canadian employees under a defined contribution plan. The total expense for the plan amounted to \$1,168,000 (2000 - \$662,000).

14. Segmented information

The Company is organized and managed as a single business segment, being the provider of commercial manufacturing and pharmaceutical development services (note 1).

Canadian and foreign operations consist of the following:

	2001		
	Canada \$	Europe \$	Total \$
Revenues			
Domestic	41,922	153,721	195,643
U.S.A.	101,900	1,078	102,978
Other geographic areas	17,899	3,357	21,256
Total revenues	161,721	158,156	319,877
Capital assets	110,135	115,913	226,048
Goodwill	3,456	—	3,456

	2000		
	Canada \$	Europe \$	Total \$
Revenues			
Domestic	24,015	152,241	176,256
U.S.A.	75,579	—	75,579
Other geographic areas	1,933	2,541	4,474
Total revenues	101,527	154,782	256,309
Capital assets	61,489	89,999	151,488
Goodwill	3,638	—	3,638

During the years ended October 31, 2001 and 2000, three (2000 - two) clients accounted for more than 10% of the Company's total revenues. As a percentage of total revenues, these clients amounted to 31%, 15% and 13% (2000 - 37% and 18%).

Revenue information by service activity is as follows:

	2001 \$	2000 \$
Commercial manufacturing – prescription	208,547	172,892
Commercial manufacturing – over-the-counter	77,692	62,133
Development services	33,638	21,284
	319,877	256,309



1, 2, 3

Mr. Green is currently Chairman of the Board of Patheon Inc. He is also Chairman of the Board of Trustees of the Superior Propane Income Fund and a Director of Superior Propane Inc. and The Gore Mutual Insurance Company. Mr. Green has been Chairman of the Board of Patheon Inc. since 1996.



Mr. Tedford has been CEO of Patheon Inc. since 1996. He joined Patheon in 1992 as CFO, a position that he still holds. Mr. Tedford previously held senior management positions in one of Canada's leading international accounting firms. He is a graduate of McGill University and Harvard Business School's Advanced Management Program and is a Chartered Accountant. He has been a Director of Patheon since 1992.



Mr. DiPietro is President and COO of Patheon Inc. He joined Patheon in 1982, becoming President of the Niagara Region and Burlington operating divisions in 1989. He was appointed to his current position in 1996. Mr. DiPietro holds an Honours B.Sc. in Biochemistry and an MBA from McMaster University. He has been a Director of Patheon since 1993.



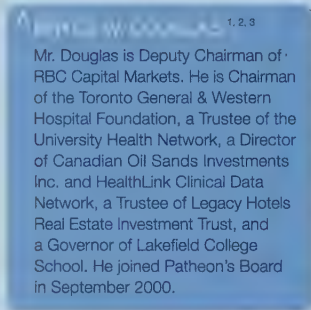
Mr. Arnett is Counsel to the law firm Fraser Milner Casgrain LLP. He served as President and CEO of Molson Inc. from 1997 to 2000 and previously was a senior partner with the law firm Stikeman Elliott in Toronto. Mr. Arnett has a B.A. and an LL.B. from the University of Manitoba. He received a Master of Laws from Harvard University in 1964. He joined Patheon's Board in March 2001.



BOARD OF DIRECTORS



The Honourable Roy MacLaren, P.C. served as the High Commissioner for Canada to the United Kingdom of Great Britain and Ireland from 1996 to 2000 and was formerly Canada's Minister of International Trade. He is currently a Director of several public companies, including Standard Life, Brascan Inc. and Canadian Tire Corporation. He joined Patheon's Board in January 2001.



Mr. Douglas is Deputy Chairman of RBC Capital Markets. He is Chairman of the Toronto General & Western Hospital Foundation, a Trustee of the University Health Network, a Director of Canadian Oil Sands Investments Inc. and HealthLink Clinical Data Network, a Trustee of Legacy Hotels Real Estate Investment Trust, and a Governor of Lakefield College School. He joined Patheon's Board in September 2000.



1, 2

Mr. Ploder is President and CEO of Vital Retirement Living Inc. and a Director of a number of private companies. He previously served as President & CEO of Bracknell Corporation from 1989 to 1999. Mr. Ploder is a Chartered Accountant and has been a Director of Patheon since 1992.



1, 3

Mr. Watchorn is a senior partner of the law firm Davies Ward Phillips & Vineberg LLP, of which he became a partner in 1970. In January 1999, he joined TrizecHahn Europe in London, England as Executive Director, and returned to Davies Ward Phillips & Vineberg LLP in September 2001. Mr. Watchorn has been a Director of Patheon since 1998.

The Corporate Governance Committee regularly reviews the Corporation's governance policies and practices with the Board and management. Details of these practices are communicated to shareholders in the Notice of Meeting and Management Proxy Circular for the Annual and Special Meeting of Shareholders.

- ¹ Corporate Governance Committee
- ² Audit Committee
- ³ Compensation and Human Resources Committee

SENIOR MANAGEMENT

ROBERT C. TEDFORD*
CHIEF EXECUTIVE OFFICER
CHIEF FINANCIAL OFFICER

NICK A. DIPIETRO*
PRESIDENT
CHIEF OPERATING OFFICER

SHABBIR T. ANIK, PH.D.*
EXECUTIVE VICE-PRESIDENT,
PDS & CHIEF SCIENTIFIC
OFFICER

CLIVE V. BENNETT*
EXECUTIVE VICE-PRESIDENT,
OPERATIONS

ALDO BRACA*
EXECUTIVE VICE-PRESIDENT,
EUROPEAN BUSINESS
DEVELOPMENT & PRESIDENT,
PATHEON ITALIA S.P.A.

MARTIN W. HEIKOOP*
EXECUTIVE VICE-PRESIDENT

MICHAEL S. HARDING
SENIOR VICE-PRESIDENT,
QUALITY & TECHNICAL AFFAIRS

RONALD B. MITCHELL, C.A.*
SENIOR VICE-PRESIDENT,
FINANCE & TREASURER

RON J. QUON
SENIOR VICE-PRESIDENT,
HUMAN RESOURCES,
ENVIRONMENTAL,
HEALTH & SAFETY

RICCARDO TRECROCE*
GENERAL COUNSEL,
SECRETARY & SENIOR
VICE-PRESIDENT,
CORPORATE ADMINISTRATION

TOM L. FERGUSON
VICE-PRESIDENT,
INFORMATION TECHNOLOGY

* OFFICER OF THE COMPANY

MANAGEMENT ADVISORY BOARD

Established in 1999, the Management Advisory Board provides strategic counsel to Patheon's senior executives on current developments in the global pharmaceutical industry – guiding the Company toward achieving the leadership position in the outsourcing of pharmaceutical manufacturing and development services.

G. JOE BLAKER, Ph.D. **Independent Director and Business Advisor**

In 1999, Dr. Blaker joined Patheon's Management Advisory Board. Previously, he served as worldwide head of pharmaceutical and fine chemical manufacturing operations for Glaxo Wellcome, responsible for 53 manufacturing sites employing more than 18,000 people. Dr. Blaker serves as a non-executive director of a number of public companies, including Rhodia ChiRex Inc. and Weston Medical Group plc. In addition, he acts as advisor to several other pharmaceutical and chemical companies and is currently Chairman of the UK Government's Chemicals Foresight Panel. Dr. Blaker resides in Beaconsfield, England.

MR. RUDOLF MEYER **Business Advisor**

Mr. Meyer joined Patheon's Management Advisory Board in January 2002. An experienced pharmaceutical industry executive, Mr. Meyer served F. Hoffmann-La Roche during a distinguished 32-year career, most recently as Senior Vice-President of Global Supply Chain and Manufacturing. Mr. Meyer is fluent in German, English, French and Spanish and currently resides near Basel, Switzerland.



< Toronto Region Operations
2100 Syntex Court
Mississauga, Ontario L5N 7K9
Canada
Tel.: (905) 821-4001
PETER D. SAULL
SITE DIRECTOR

- 492 employees
- 239,500 square feet
- High potency, solid, semi-solid and liquid dosage forms



< Toronto York Mills Operations
865 York Mills Road
Toronto, Ontario M3B 1Y5
Canada
Tel.: (416) 443-9030
ROMAN B. CHARKO
SITE DIRECTOR

- 181 employees
- 160,000 square feet
- Solid, semi-solid and liquid dosage forms



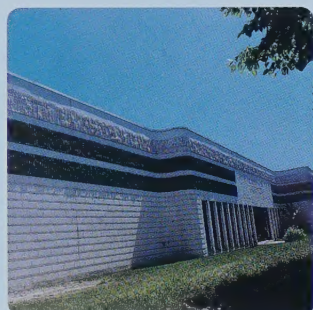
< Whitby Operations
111 Consumers Drive
Whitby, Ontario L1N 5Z5
Canada
Tel.: (905) 668-3368
JAG PATEL
SITE DIRECTOR

- 406 employees
- 192,700 square feet
- Controlled substances, solid, powder and liquid dosage forms



< Burlington Century Operations
977 Century Drive
Burlington, Ontario L7L 5J8
Canada
Tel.: (905) 639-5254
DICK RENWICK
SITE DIRECTOR

- 88 employees
- 45,000 square feet
- Solid dosage forms



^ Burlington Gateway Operations
921 Gateway Drive
Burlington, Ontario L7L 5K5
Canada
Tel.: (905) 639-4933
DICK RENWICK
SITE DIRECTOR

- 81 employees
- 22,800 square feet
- Powders



^ Niagara Region Operations
P.O. Box # 158
333 Jarvis Street
Fort Erie, Ontario L2A 5M9
Canada
Tel.: (905) 871-1870
GRANT D. GILKER
SITE DIRECTOR

- 274 employees
- 132,800 square feet
- Solid, semi-solid and liquid dosage forms

OPERATIONS: NORTH AMERICA & EUROPE



< Patheon France S.A.
Bourgoin-Jallieu Operations
40, boulevard de Champaret
B.P. 448
38317 Bourgoin-Jallieu, Cedex
France
Tel.: +33 4 7493 8700
DOMINIQUE RIVOIRE
SITE DIRECTOR

- 219 employees
- 272,000 square feet
- Liquid and solid dosage forms



< Patheon Italia S.p.A.
Monza Operations
Viale G. B. Stucchi, 110
I-20052 Monza
Italy
Tel.: +39 039 2047 1
FULVIO SMALDONE
SITE DIRECTOR

- 312 employees
- 344,000 square feet
- Sterile (liquids & lyophilized), solid and liquid dosage forms



< Patheon UK Limited
Swindon Operations
Kingfisher Drive
Covingham, Swindon
Wiltshire SN3 5BZ England
Tel.: +44 1793 524411
MICHEL GRANDJEAN
SITE DIRECTOR

- 528 employees
- 293,000 square feet
- Sterile liquids, sterile powdered cephalosporins, solid and semi-solid dosage forms

EUROPEAN BUSINESS OFFICE
Viale Algeria 79
00144 Rome
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Fax: +39 06 54 22 07 42

CORPORATE HEADQUARTERS

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2100 Syntex Court
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Fax: (905) 812-6705
E-mail: patheon@patheon.com
Web site: www.patheon.com

SHAREHOLDER ACCOUNT ENQUIRIES

Computershare Trust Company of Canada
100 University Avenue, 11th floor
Toronto, Ontario M5J 2Y1
Canada
Tel.: 1 (800) 663-9097
E-mail: caregistryinfo@computershare.com
Web site: www.computershare.com

TRANSFER AGENT AND REGISTRAR

Computershare Trust Company of Canada

INVESTOR AND FINANCIAL INFORMATION

Robert C. Tedford
Tel.: (905) 812-6768
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e-mail: rtedford@patheon.com

AUDITORS

Ernst & Young LLP

LEGAL COUNSEL

Davies Ward Phillips & Vineberg LLP,
Toronto, Canada
Macfarlanes, London, England
Studio Legale Ughi e Nunziante, Milan, Italy
Ernst & Young LLP, France

BANKERS

Canadian Imperial Bank of Commerce
HSBC Bank Canada
Banca Intesa Banca Commerciale Italiana SpA
HSBC Bank plc

DIVIDEND POLICY

The Board of Directors periodically reviews the dividend policy of Patheon Inc. The Company currently does not pay dividends on its common shares, and has no plans to do so in the foreseeable future, preferring to reinvest its cash to enhance the Company's growth.

ANNUAL MEETING

Shareholders are invited to attend Patheon's Annual and Special Meeting of common shareholders to be held at 10:30 a.m. (Eastern Standard Time) on Wednesday, March 20, 2002:

Toronto Hilton Hotel
Toronto III Ballroom
145 Richmond Street West
Toronto, Ontario
Canada

The meeting will be broadcast live over the Internet on Patheon's web site at **www.patheon.com**. An archived version of the audio webcast will be available on Patheon's web site after the meeting.

SHARE INFORMATION

as of October 31, 2001,
except recent price

Listing: Toronto Stock Exchange (TSE)

Symbol: PTI

Shares Outstanding: 50,296,000

Public Float: 49,169,000

High/Low/Close: \$16.35/\$7.60/\$10.98

Recent Price (January 31, 2002): \$11.93

PATHEON STOCK PERFORMANCE VS TSE 300

Value of \$100 invested on October 31, 1996



MORE

www.patheon.com